REPORTS

OF

CURRENCY COMMITTEES

Herschell Committee of 1893
Fowler Committee of 1898
Chamberlain Commission of 1914
Babington Smith Committee of 1919

(*Reprinted in India.*)

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TABLE OF CONTENTS.

REPORT OF THE INDIAN CURRENCY COMMITTEE.

Analysis of the Report.

Report of the Indian Currency Committee, 1893.

INDIA OFFICE,
31st May 1893.

To

THE RIGHT HONOURABLE THE EARL OF KIMBERLEY, K.G.,
SECRETARY OF STATE FOR INDIA,

Statement of the Question.

1. Question referred to the Committee.—The question referred to the Committee by Your Lordship is whether, having regard to the grave difficulties with which the Government of India are confronted through the heavy fall in the gold value of silver, it is expedient that Her Majesty's Government should allow them to carry into effect the proposals which they have made for stopping the free coinage of silver in India with a view to the introduction of a gold standard. And if we are of opinion that there is no sufficient ground for overruling the Government of India, but that the measures by which they propose to attain their object require modification, we are asked to offer any suggestion that we think fit for the purpose.

2. Points to be considered.—The expediency of allowing the Government of India to carry into effect the proposals which they have made must depend on the view of the present and future situation of that Government as regards their revenue and expenditure as well as upon a just estimate of the effect of a varying and possibly much lower exchange upon the commerce and people of India.

Financial difficulties of the Government of India.

3. Increase in number of rupees needed to discharge gold obligations.—There can be no doubt that the Government of India have experienced serious difficulty owing to the fall of exchange which has been going on for many years. The Government have yearly to remit a very large sum to this country in discharge of their gold obligations. In 1873-74, before the fall commenced, the amount remitted was 13,285,678*l.*, which, at a rate of exchange of 1*s.* 10·351*d.*, was represented by Rx. 14,265,700. During last year (1892-93) the amount remitted was 16,532,215*l.*, which, the average rate of exchange in that year, *viz.*, 1*s.* 2·985*d.*, required a payment of Rx. 26,478,415. If this could have been remitted at the exchange of 1873-74, it would have needed only Rx. 17,751,920. The whole of this difference of Rx. 8,726,495 cannot properly be regarded as a loss to the Government of India arising from the difference in exchange. It is certain, however, that India had

actually to remit in 1892-93 upwards of Rx. 8,700,000 more than if the exchange had been at its former point.

4. Consequent present deficit.—At an estimated exchange of 1*s.* 4*d.* per rupee for the past year, a surplus of revenue over expenditure was shown of Rx. 146,600; the exchange having fallen to an average of rather less than 1*s.* 3*d.*, this surplus has been converted into an estimated deficit of Rx. 1,081,900, notwithstanding the improvement of the revenue by Rx. 1,653,300 over the Budget Estimate.

5. Prospect of further fall in exchange.—Nor is this all. The Government are compelled to contemplate a further fall, the effect of which cannot be forecast. There has been for some years past an almost continuous fall in exchange, though it was varied by a sharp rise in the year 1890. The average rate in 1889-90 was 1*s.* 4·566*d.* In 1890-91 the average rate was 1*s.* 6·089*d.* But in 1891-92 it fell to 1*s.* 4·733*d.*, in 1892-93 to 1*s.* 2·985*d.*, and exchange has been of late scarcely maintained at 1*s.* 2$\frac{5}{8}$*d.* by the refusal to sell bills on India below that rate. The extent to which the financial position of the Government of India is affected by exchange is emphasised in the following passages of the recently published statement of Sir David Barbour:

Sir D. Barbour on the situation.—"The immediate cause of our financial difficulties, and the cause which, by comparison and for the time being, dwarfs all others, is the fall in the gold value of silver, which, as I have already shown, has added to the Indian expenditure in two years more than four crores of rupees. If that fall could be stayed and the rate of exchange with England fixed permanently at even its present low figure, the difficulty of dealing with the present deficit would be comparatively light. The revenue continues to grow in a satisfactory manner; even under the influence of indifferent seasons and poor harvests, it has made fair progress. If we could feel assured that there would be no further fall in exchange, I have little doubt that increase of revenue, restriction and reduction of expenditure with possibly some taxation of a temporary nature, would in a very short time re-establish equilibrium. A serious effort would no doubt be required in the first instance, but with a fixed rate of exchange we would have a definite task before us, and our measures could be regulated accordingly. But it unfortunately happens that, unless some settlement of the currency question is obtained, there is no prospect of even the most moderate degree of stability in the rate of exchange.

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"Our financial position for the coming year is at the mercy of exchange, and of those who have it in their power to affect in any way the price of silver. If we budget for the present deficit of Rx. 1,595,100, and exchange rises one penny, we shall have a surplus; if it falls a penny, we shall have a deficit of more than three crores; if we impose taxation to the extent of one and a half crores of rupees, a turn of the wheel may require us to impose further taxation of not less magnitude; another turn, and we may find that no taxation at all was required. It will be obvious from what I have just said that what we have got to consider in making our arrangements for next year is not so much the question of increasing the public revenue or restricting that portion of the public expenditure which is under our control, but the chances of a settlement of the currency question."

Value of Silver.

6. Recent production of silver.—The production of silver has largely increased of late years, as will be seen from the following table, based as regards the earlier years on the statistics compiled

by Professor Soetbeer, and as to the more recent years on the reports of the Director of the Mint in the United States:

Average annual production of silver.	Kilos.	Approximate equivalent in ounces at 32·15 to the kilogramme.
1876 to 1880	2,450,252	78,776,000
1881 to 1885	2,812,908	90,435,000
1886 to 1890	3,459,201	111,213,000
1890	4,144,233	133,237,000
1891	4,493,100	144,453,000
1892	4,731,000 to 4,900,000	152,102,000 to 157,535,000

7. Bland Act in United States.—In the year 1878 what is known as "the Bland Act" was passed by the Legislature of the United States, which required the Government of that country to purchase not less than 24,000,000 and not more than 48,000,000 dollars' worth of silver per annum, which would be equal to a consumption vairying from 20,625,000 to 41,250,000 ounces (641,000 to 1,283,000 kilos.) in the year. Under the authority of that Act the Government purchased yearly the minimum amount required. Notwithstanding these purchases, the price of silver fell from $52\frac{9}{16}d.$ per ounce, the average of 1878, to $43\frac{11}{16}d.$ in February 1890.

8. Sherman Act.—In that year what is known as "The Sherman Act" was passed by the United States Legislature, under which the duty was imposed on the Government of purchasing no less than 54,000,000 ounces (1,680,000 kilos.) a year in lieu of the amount required to be purchased under the Bland Act.

9. Rise in value of silver in 1890.—The effect of this obligation to purchase silver to the value of about six millions sterling beyond the purchases required under the earlier law, coupled probably with the anticipation that further legislation, and perhaps free coinage of silver, would follow, was a sudden and considerable rise in the value of silver, which culminated in the month of September 1890, when it reached the price of $54\frac{5}{8}d.$ per ounce. There was, however, a speedy decline from this price, and since July 1892 silver has realised not more than an average of $38\frac{1}{2}d.$ per ounce, the present price being $37\frac{11}{16}d.$

10. Effect of American legislation and Indian imports on value.—Even if the increased production is kept in view, it is not easy to understand why, with the increased purchasing by the United States to the amount of six millions sterling per annum, and the simultaneous large increase of the Indian imports of silver, which averaged from August 1890, when the Sherman Act came into force, to March 1893, upwards of 46,500,000 ounces, the price should be six pence per ounce lower than it was in the beginning of 1890. It has, indeed, been argued that the recent fall in the price of silver was due to the blow which the passing of that

Act gave to the hopes of those who desired the free coinage of silver. But against this it is to be observed that the price of silver in London rose during the time that the Sherman Act was passing through Congress, and continued to rise for some weeks after it became law. Whatever be the cause, the fact that, although the United States Government have under that Act made purchases varying from 34 to 42 per cent. of the estimated production of the world, and India has increased and not diminished her imports of the metal, the price of silver has fallen to its present low level is beyond question and of grave moment.

11. Further fall in value of silver to be expected.—Supposing even that no change were made in the currency arrangements of the United States, the experience of the past would forbid the conclusion that the price of silver would be stationary at its present level. It would be imprudent to act on the assumption that no further fall is possible or even probable.

12. Brussels Conference.—The International Monetary Conference which recently assembled at Brussels has not led to any change in the situation, and, although it adjourned to a future day, that day is now past, and it seems uncertain whether there will be any further meeting.

13. Agitation in United States.—Moreover, a strong agitation exists in the United States with respect to the law now in force providing for the purchase of silver. Fears have been, and are, entertained that there may come to be a premium on gold, and strong pressure has been brought to bear upon the Government of that country with a view to bring about an alteration of that law.

14. Possible repeal of Sherman Act.—In December last a Bill was introduced in the Senate to repeal the Sherman Act, and another to suspend purchases under it. Whether any such measure will pass into law it is impossible to foretell, but it must be regarded as possible; and although in the light of past experience predictions on such a subject must be made with caution, it is certainly probable that the repeal of the Sherman Act would be followed by a heavy fall in the price of silver.

15. Increase in production notwithstanding fall in price.—Opinions differ as to the fall in price which would be effectual largely to check the production of silver. From time to time, as the price of silver has continued to fall, the opinion has been expressed that the point had been reached at which production must be checked. Experience has, however, falsified all these predictions. It is, of course, true that the fact that the working of a mine has become unprofitable does not ensure that the output shall be at once diminished or the mine closed. But, if this state of things were long to continue, and owing to a progressive fall in the price of silver mining operations could only be carried out at an increasing loss, one would expect to find the working abandoned before any very long period had elapsed. It is, however, remarkable that a period of continually increasing fall in the price

of silver has been coincident with a large increase in the production of that metal. In the quinquennium 1876—1880, the annual average price of silver ranged from $54\frac{13}{16}d.$ to $51\frac{1}{4}d.$, the average for the quinquennium being $52\frac{3}{4}d.$ In the next quinquennium, 1880—1885, the range was from $51\frac{11}{16}d.$ to $48\frac{5}{8}d.$, the average for the quinquennium being $50\frac{5}{8}d.$, whilst from 1886 to 1890 the price ranged from $47\frac{11}{16}d.$ to $42\frac{11}{16}d.$, the average for the quinquennium being $44\frac{5}{8}d.$ And yet the annual average production of silver at the last quinquennium was 3,459,201 kilos. (111,213,000 ounces) as compared with 2,450,252 kilos. (78,776,000 ounces) in the quinquennium 1876—1880, being an increase of 41 per cent. And with an average price in 1891 of $45\frac{1}{16}d.$ and in 1892 of $39\frac{13}{16}d.$, or an average for the two years of $42\frac{7}{16}d.$, the production of 1891 has been estimated at 4,493,100 kilos. (144,453,000 ounces) and that of 1892 at 4,731,000 to 4,900,000 kilos. (152,102,000 to 157,535,000 ounces). This may show that, even at the present price, the production of silver is still profitable in a large proportion of the mines, and that in some it is sufficiently so to stimulate increased development, and that even a further fall would not necessarily diminish the total output. The phenomena may, indeed, be partly accounted for by the circumstance pointed out in the Report of the Gold and Silver Commission that investments in the mines of precious metals are largely of a speculative character, and that many such mines may be opened out and worked for a considerable time at a loss in the hope that such rich deposits of the ore will be found, or that altered circumstances may so change the value of the metal that great gains will be reaped in the future.

16. Effect of further fall on remittances of Government of India.—A review of the changes in the price and production of silver which have characterised the last 12 years certainly forbids our entertaining any confidence that, if a further heavy fall in the price of silver were to take place, it would be, at any point capable of estimation, checked or counteracted by diminished production. It must be remembered, as pointed out by the Gold and Silver Commission, that the effect of throwing a large quantity of silver upon the silver market is not to be measured by the proportion which that quantity bears to the whole stock of silver in the world, but by the proportion which it bears to the stock of silver in the world after deducting from that stock the very large amount of silver money now kept in circulation by countries which have a silver token currency, since all of this money circulates at an artificial value, and none of it is subject to the fluctuations of the market. It cannot be regarded then as otherwise than within the reasonable bounds of possibility that a repeal of the Sherman Act might lead to a fall in the price of silver of even 6*d.* per ounce or more, and that there might be no substantial reaction from the level thus reached. Such a fall would, it may be said with practical certainty, reduce the exchange to about 1*s.* 0*d.* per rupee, and involve the necessity of raising at least Rx. 6,612,000 more than would be required by the Government of India to effect, even at the rate of

exchange of 1*s*. 3*d*. per rupee, a remittance of the amount drawn last year, namely, 16,530,000*l*., while the payment of 19,370,000*l*., which is the present estimate of the drawings for 1893-94, would, at 1*s*. 3*d*. per rupee, require Rx. 30,992,000 and at 1*s*. 0*d*. per rupee Rx. 38,740,000, involving an increase of Rx. 7,748,000.

Claims of Indian officials.

17. Servants of Government.—The difficulties which the Indian Government have in meeting the Home charges are aggravated by the fact that the fall in exchange has led to claims on the part of their officers, civil and military, who receive salaries in rupees, to some compensation for the loss which they sustain owing to the fall in exchange. Many of those officials are under the necessity of remitting a considerable portion of their income to this country for the support of their families and the education of their children. It has been said that prices have fallen in this country during the last 15 years, and that a smaller sterling remittance will now purchase more than formerly. This is no doubt to some extent true, but it does not apply to all prices. It is a matter of dispute how far the fall of prices in this country compensates for the smaller sterling remittance which the same number of rupees will procure; but it is certain that, when due allowance has been made for this, the purchasing power of the incomes of Indian officials has been largely reduced.

18. Practice of private employers.—It appears that some European employers have felt themselves bound to make an allowance to the Europeans in their service in India sufficient to counterbalance to some extent the loss which they experience owing to the fall of the rupee; and there can be little doubt that even in existing circumstances, and still more if the fall of exchange continues, the Government of India cannot turn a deaf ear to the appeals of their servants for similar treatment without the danger of engendering serious discontent, apart from the question whether such appeals are just and reasonable.

Expansion of Revenue.

19. Expansion of revenue hitherto.—Hitherto the expansion of the revenue has largely provided for the additional calls which the fall of exchange has made on the Government of India. There has been, in spite of these additional calls, an average surplus during the last 10 years of Rx. 261,550. It is true that, but for the expenditure rendered necessary by the fall in exchange, there might have been further remissions of taxation, and more might profitably have been spent upon public works. Though upon the whole the Government have not been compelled to impose increased taxation in order to discharge their liabilities whilst the fall in exchange has been in progress, certain alterations have been made in the taxation of the country—some in the direction of remission, others of an increase—with the net result that amount of the increase

has not greatly exceeded the amount of the remission. But it is noteworthy that, whilst the remissions were all prior to 1882, the increased taxation has for the most part been imposed since that date. The addition to the salt tax, which was the principal source of increased revenue, produced a sum of Rx. 1,725,000.

20. Cannot be relied upon to meet future deficiencies.—In the past year the fall in exchange of about one penny has added Rx. 1,635,300 to the expenditure with the result of an expected deficit of Rx. 1,081,900 instead of the anticipated surplus; and the rate in 1893-94 being estimated at 1*s.* 2¾*d.* per rupee, an addition of Rx. 2,229,400 is caused to the expenditure beyond the charge for exchange entered in the Budget of March 1892. If a further heavy fall in exchange were to take place, it is impossible to expect that a financial equilibrium would be brought about by an expansion of the revenue alone.

Effect of fall in Exchange on the people of India and its Commerce.

21. Effect of fall in Exchange on the people of India.—Before considering how the Government of India can meet the difficulties which they experience, and which they feel compelled to anticipate, it will be well to enquire what effect the variations in exchange to which attention has been called have produced upon the commerce of India and the prosperity and condition of its people.

22. Effect on the remittance of produce.—In estimating the effect upon the people of India of its being necessary to raise an increased number of rupees to meet the sterling remittances of the Government of that country, it must be borne in mind that the extent of the burthen imposed upon the people of India by these remittances is measured by the quantity of produce which they represent, for it is by the export of the produce that the debt is in reality discharged. In so far as the necessity of exporting more produce arises from the circumstance that gold prices are lower, the people of India are in the same position as those of Australia or any other country which has to export produce for the purpose of paying the interest on its gold debt. The question to be considered is, what effect has the fall in exchange upon the amount of produce which must be exported to meet a given gold liability? To determine this, the gold price of the produce must be assumed to be stationary. When silver falls in relation to gold, the greater number of rupees which is required to meet a given gold payment will not represent a greater quantity of produce than before, if the silver price in India of the produce exported responds to the changed value of silver in relation to gold, *i.e.*, if it has risen, or has been prevented from falling. Silver prices must ultimately thus respond, although an interval may elapse before the correspondence is complete; and during this time, whilst more produce is exported, the Indian ryot is getting proportionately less in silver for his produce. It has indeed been alleged that the fall in the gold price of certain Indian products is to be attributed to the fall in the value of the rupee, but

this allegation is strongly controverted; and, having regard to the phenomena presented in the case of Indian products not greatly open to competition, and to the necessary effect of competition in the case of those which are within the sphere of its influence, it seems far from clear that the fall in the gold price of Indian products would have been materially less if the exchange had not fallen.

23. Transfer of burdens from one class to another.—Even if the burden upon the people of India as a whole has not been increased by the fall in exchange, there can be no doubt that it has been to some extent shifted from one class to another. The burden of those who pay a fixed land revenue under a permanent settlement has been lightened, and the same may be said of all those whose land revenue has not been resettled in recent years, or resettled with adjustment to meet the most recent conditions. On the other hand, the increased salt tax presses upon the people at large, and renders more heavy the taxation of those who for the most part have suffered rather than benefited from the higher rupee prices due to the fall in the gold value of silver.

24. Effect on commerce.—We pass now to consider the manner in which the commerce of India is alleged to have been injuriously affected by the variations in exchange.

25. Harassment of trade by fluctuations.—It is said that legitimate trade is replaced by mere speculation and gambling. There seems to be a common agreement amongst those who differ in their views upon almost all other points that trade is seriously harassed by these fluctuations, though the estimates do not all agree as to the character and the extent of the inconvenience arising from this cause. It does not appear to be certain, even in the view of those who are most strongly sensible of the mischievous effect of fluctuations of exchange, that the volume of trade over a series of years has been diminished from this cause, though there seems a common agreement that any sudden or violent fluctuation almost paralyses business for a time. It is to be observed that it is not so much the fall of exchange which is complained of as the fluctuations, whether in one direction or the other. Some of those who admit the mischief to trade of exchange fluctuations allege that the extent of the mischief is not serious, since provision can be largely made against the effect of those fluctuations through the medium of banks; but it is clear that the traders cannot completely safeguard themselves in this way, and that such security as they obtain in this respect must be paid for. It must be remembered that before the fall in the price of silver began, and the fluctuations in the rate of exchange dependent upon it, the rates of exchange varied very considerably during particular years, though, no doubt, the fluctuations have been much more frequent and considerable since that time.

26. Fluctuations add to the risks of trade.—Upon the whole, it cannot be doubted that it would be well if commerce were free from the inconveniences of fluctuations which arise from a change in the relation between the standard of value in India and

in countries with which her commerce is transacted. It must not be assumed that the adoption of the same standard for the United Kingdom and India would remove all the disquieting causes of the disturbance of trade of which complaint is made. If the commodity which lies behind the exchange transaction is one that continues to fall in relation to gold, the risk which arises from bargains in a falling market will still be present. The liability of the standard of the one country to fall in relation to the other causes, however, an additional risk, and consequently increased disturbance to trade.

27. Alleged stimulation of exports by fall in exchange.—It is said that the tendency of a falling exchange is to stimulate exports; that, inasmuch as more silver, *i.e.*, a higher silver price, is received in respect of the same gold price, whilst wages and the other factors in the cost of production do not increase in the same proportion, production becomes more profitable, and is therefore stimulated. Assuming this to be true, the effect of each successive fall must be transitory, and can continue only until circumstances have brought about the inevitable adjustment. Although one may be inclined, regarding the matter theoretically, to accept the proposition that the suggested stimulus would be the result of a falling exchange, an examination of the statistics of exported produce does not appear to afford any substantial foundation for the view that in practice this stimulus, assuming it to have existed, has had any prevailing effect on the course of trade; on the contrary, the progress of the export trade has been less with a rapidly falling than with a steady exchange. For example, from 1871-72 to 1876-77 the gold value of the rupee fell constantly from 23·126*d.* to 20·508*d.*, or about $11\frac{1}{4}$ per cent.; the exports of merchandise were actually less in the latter year than in the former, although in 1876-77 their rupee value exceeded by about 10 per cent. that of the exports of either 1870-71 or 1872-73. From 1878-79 to 1884-85 exchange was fairly steady, the average rates varying only between 19·961*d.* and 19·308*d.* per rupee, or about $3\frac{1}{4}$ per cent.; and during those six years the exports rose by no less than $36\frac{1}{2}$ per cent. Again, between 1884-85 and 1888-89 the fall of the rupee was very rapid, from 19·308*d.* to 16·379*d.*, or over 15 per cent., and the exports increased during those four years by $16\frac{1}{2}$ per cent.; but in the single year 1889-90, when there was a slight improvement in the exchange, the exports increased by more than $6\frac{1}{2}$ per cent. It is said, too, that, whilst a falling exchange tends to stimulate exports, there is a corresponding tendency to check imports. Here again statistics do not seem to show that diminished imports have been coincident with a lower exchange. Taking the same periods as before, from 1871-72 to 1876-77, when exchange fell $11\frac{1}{4}$ per cent., imports of merchandise into India increased by 17 per cent.; from 1878-79 to 1884-85, when exchange was steady, the increase of imports exceeded 47 per cent.; between 1884-85 and 1888-89, when the rupee fell about 15 per cent., the imports were augmented by nearly 25 per cent.; while in 1889-90, when exchange slightly rose, the imports were rather less than in the previous year. Upon the whole

we cannot see any evidence that the effect of a falling exchange on the country at large in influencing either exports or imports has over a series of years been very considerable. Some trains of *a priori* reasoning would seem to lead to the same conclusions, and also to the further conclusion that, even if a fall in the gold value of the rupee does stimulate exports, the result is not necessarily to the benefit of India as a whole, though it may temporarily benefit the employer at the expense of the wage-earner, because wages rise more slowly than prices.

28. Check to investments in India.—The want of a stable exchange between England and India, and the fact that it has fallen so heavily, has, it is alleged, greatly checked the investment of British capital in India and the development of the country which would have been the fruit of such investments. London is the lending market, and London thinks in gold. London is ready enough to lend upon contracts for repayment in gold, but hesitates to enter upon silver transactions, or to engage in industrial enterprises in a silver country. There can be no doubt that uncertainty as to the interest which would be received for the investment, and as to the diminution which the invested capital might suffer if it were desired to retransfer it to this country, tends to check British investments in India. This is a real evil, the importance of which we do not desire to underrate. It has been pointed out, however, that a great number of industrial enterprises have been established in India during recent years, such as collieries, cotton mills, jute mills, woollen mills, and paper mills, in which much capital has been invested; and that large sums have been spent upon tea plantations is evidenced by the enormous increase in the quantity of tea grown in and exported from India. And it must be remembered that the adoption by India of the same standard which exists in England might not remove all obstacles to the investment of capital in that country. Capitalists have of late been slow to invest in many kinds of industrial enterprise owing to the fact that prices are falling or have fallen very generally. If a gold standard were adopted for India, and similar phenomena of falling prices ensued there, capitalists might still be unwilling to provide capital for industrial enterprises. In connection with the point under discussion, it may be well to observe that a falling exchange, owing to its effects upon their salaries, savings, and pensions, renders it more difficult to procure and arrange for the services of the European employés required for the carrying on of industrial undertakings in India.

29. Attraction of open mints for depreciating silver.—There is another point which ought not to be passed over in silence. It is said that by making silver the standard, and keeping the Indian mints open to silver, the Anglo-Indian Government have attracted to India that depreciating metal, and have thus made India purchase at a comparatively high cost an enormous quantity of it, which is now of less value than when it was bought. In this there is some truth, but also much exaggeration. There can be no doubt that an open mint in India offers a market into which silver could

be continuously poured without regard to the currency requirements of India until such an alteration in prices of commodities was brought about as to make its importation no longer profitable. It is only when and so far as the opening of the mints to silver has led to the importation and coinage or hoarding of useless and now depreciating silver that the free coinage of silver can be considered to have inflicted a loss upon India. What this loss amounts to we cannot determine, but we are not without indications that India is becoming surfeited with silver.

30. Recent imports and coinage of silver.—The net imports of silver into India in the 23 years from 1870-71 to 1892-93 have been Rx. 165,226,000, or an average of Rx. 7,184,000 a year, and the coinage demands have amounted to upwards of Rx. 6,500,000 annually, so that we may infer that nearly the whole of the newly imported silver has during these years passed through the mint. Since 1877-78 the net yearly imports ranged from about 4 to 11 millions Rx.; but in 1890-91 there was an abnormal rise to more than 14 millions. Much of this silver appears to have remained in the Currency Department, causing at the same time a great and sudden inflation of the paper currency. Between March and December 1890 the note issue increased from about 15¾ crores of rupees to 27 crores, an increase of 71 per cent. The inflation was yet further aggravated, and at the end of August 1892 the notes issued stood at more than 29 crores; but, according to recent returns, there has been some contraction, and the amount in circulation is now about 26 crores. With this sudden expansion of the issue of notes a corresponding increase in the silver coin and bullion reserve took place, *viz.*, from Rx. 9,771,782 at the end of March 1890 to Rx. 21,440,022 at the end of January 1891, an addition of more than 11½ crores of rupees.

Export of gold.—It deserves notice in connection with this subject that throughout 1892 the import of gold not only ceased to be in excess of the exports, but the current was reversed. During the five years ending with March 1890 the average net import was about Rx. 3,000,000. In 1890-91 it was Rx. 5,636,172, in 1891-92 it was Rx. 2,413,792, whilst in 1892-93 the net import ceased, and the excess of exports was upwards of Rx. 2,800,000.

31. Prices in India seem to be rising.—Down to a comparatively late date it was generally believed that, notwithstanding a fall in the gold value of silver, prices in India had been practically unaltered; but the evidence before us points to the conclusion that during recent years the silver price of Indian produce has risen. If, as experience shows, wages respond more slowly to the alteration in the value of the standard, this rise in the price of produce must have been prejudicial to the wage-earning classes.

32. Import of useless silver injurious to India.—The above facts give reasons for believing that the recent fall in silver, coupled with the open mint, has led India to import and coin more silver than she needs, and the worst of the evil is that it is a growing one. Every unnecessary ounce of silver which has been, or is

being, imported into India is a loss to India so long as silver is depreciating in gold value; for it is, *ex hypothesi*, not needed for present use, and it can be parted with only at a sacrifice. So far as the open mints attract unnecessary silver to India, they are inflicting a loss upon the people of the country, and benefiting the silver-producing countries at the cost of India.

33. Effects if fall should continue.—So far, we have dealt only with the past. We have now to consider the effect to be anticipated from a continued, and not improbably heavy, fall in the exchange between India and England.

34. Existing evils would be intensified, and increase of taxation become necessary.—All the evils to which attention has been called would, of course, be aggravated and intensified. If prices continued to rise, while wages were more slowly advanced, the material condition of the wage-earning class would be continually deteriorating. As respects the Government, we have already pointed out that, if no change be made in the currency arrangements of the country, and a heavy fall were to take place, such as we have referred to as possible, they would, unless they could largely reduce their expenditure, be compelled, in order to meet the increased demands upon them, to impose increased taxation to a very serious extent. It has been suggested that economy in the civil and military administration of India is still possible, a point which does not fall within the scope of our inquiry; but, even assuming that the expenditure of the Indian Government might without impairing efficiency of administration be diminished, it cannot be supposed that this could be done suddenly to a very great extent, so as to meet the anticipated difficulty. The net expenditure of the Government of India is about Rx. 50,000,000. Supposing the deficiency which had to be met should be from Rx. 8,000,000 to Rx. 10,000,000, it is not conceivable that an equilibrium could be brought about by reducing the expenditure. When we pass to consider whether the revenue required to meet the deficiency might be raised by increased taxation, we encounter at once a position of great delicacy. There is no doubt that in several directions increased taxation is possible, but the difficulties connected with it are grave, and its political danger is said to be a matter of serious moment.

Possibility of increasing taxation.

35. Existing taxes. Land revenue.—Inasmuch as the Indian producer has so far benefited by the fall in exchange that he has received a higher silver price for his produce than would otherwise have been the case, and the burden of the land revenue he has to pay has thus become less, it would be natural to seek in an increase of the land revenue a large contribution towards the deficiency. Nearly one-fourth of the land revenue is, however, permanently settled. Of the remainder the greater part is fixed on assessments for 30 years, most of which are of recent date. It is impracticable, therefore, to derive from this source the revenue required.

36. Salt tax.—An increase of the salt tax has been before now resorted to for the purpose of obtaining additional revenue. But the objections to this tax have long been recognised. It is in the nature of a poll-tax, which falls on all classes, but presses most heavily on the very poor. It is true that the price of salt has been reduced in recent years, but the tax is now about 600 per cent. *ad valorem*, and any increase would chiefly affect those who have suffered rather than benefited by the fall in exchange. It has been strongly pressed upon us, too, that it is the main reserve of taxation in case of war or any other emergency, and that it ought not to be exhausted in order to meet the present difficulty. Even an addition of 20 per cent. to the existing tax would not yield more than from Rx. 1,500,000 to Rx. 1,750,000.

37. Stamp duties.—An addition to the stamp duties is deprecated on the ground that they are largely a tax on the administration of justice, and that it would not be right materially to augment taxation of this description.

38. Excise.—Doubts are entertained, and probably with reason, whether it would be possible to raise a largely increased revenue by means of excise. It is said that it would stimulate illicit practices, and any attempt to augment the excise revenue would be attacked, as calculated to increase drinking and to promote intemperance.

39. Import duties.—Of all the suggested methods of adding to the revenue, the reimposition of import duties would, according to the evidence before us, excite the least opposition; indeed, it is said that it would even be popular. The duties on cotton goods have, however, only recently been abolished. They were the subject of vehement attack in this country. Any attempt to reimpose them would meet with great opposition. And it cannot be denied that the reimposition of such duties would provoke a demand for a countervailing excise upon all cotton goods manufactured in India. Although such an excise duty might be collected without serious difficulty in respect of goods manufactured in the cotton mills of Bombay and elsewhere, it is alleged that it would be wholly impracticable to enforce it generally in view of the extent to which the manufacture of cotton goods on a small scale prevails throughout India.

40. Export duties.—The arguments urged against the reimposition of export duties are strong and sound in principle. The only duty of that description now in force is imposed on the export of rice. Any increase of it is said to be impracticable in view of the competition of other countries; the desire of the Government of India to abolish it has been often expressed; and it is even doubtful whether the existing duty can be maintained.

41. Income tax.—If the income tax were raised to twice its present rate, it would probably produce about Rx. 1,500,000 more than it now does. The minimum income liable to the tax is Rs. 500. An increase in the rate would produce very great discontent amongst

those who are capable of appreciating and criticising the actions of the Government, and of promoting agitation when they are prejudicially affected. It must be borne in mind, too, that the class which suffers most from the fall in exchange would be most affected by an increased income tax.

42. New taxes. Sugar and tobacco.—We have passed in review the means of taxation which have been, or are now, in use in India. It remains to consider the new sources of taxation which have been suggested. The only articles so largely consumed that taxation of them would afford the prospect of any great augmentation of the revenue are tobacco and sugar. These are grown very generally throughout India in small quantities. To procure a revenue from them by means of taxation would involve constant and vexatious interference with the people, and the cost of collecting and enforcing the tax would be enormous in proportion to the sum realised. Those who have given evidence on this subject, and who entertain the gravest objections to an increase of the salt tax, are nevertheless of opinion that with all its evils this would be preferable to an attempt to raise a revenue by a taxation of sugar or tobacco.

43. Succession duty.—Although it is recognised that there is much to be said in principle in favour of imposing a succession duty, the difficulties connected with its imposition are enhanced in India by the many different laws which regulate succession, and by the extent to which the family system affects the distribution of property in case of death. This has hitherto stood in the way of its introduction, and it would take a long time to develop any practical scheme; moreover, whether it would be found possible to add largely to the revenue by means of it must be matter of speculation. For these reasons it could not be adopted in order to meet the present emergency.

44. Conclusions as to increase of taxation.—We are not in a position to determine whether the apprehensions expressed to us that increased taxation cannot be resorted to without grave mischief are to the full extent well founded, or whether they are exaggerated. But it is not easy to see how the burden of the added taxation which would be requisite to counterbalance the fall in exchange could be made to rest on those who might with the most justice be subjected to it, or how the added revenue could be provided except in a manner opposed to sound principles of taxation. Even if it be thought that the political dangers anticipated are the offspring of somewhat exaggerated fears, it is at least possible that they may be under-estimated. Representations that a great increase of taxation was due to what has been erroneously called the "tribute" paid to this country would add sensibly to the danger, and afford an inviting theme for agitators. It is of importance to recognise the fact that the public revenues of India, as of most Asiatic countries, largely consist of elements of income which have not the character of taxation as that term is used in western Europe, and that it has been through the natural growth of

these revenues that the increased expenditure of recent years has been met to a considerable extent.

Possibility of reducing Expenditure.

45. Possibility of reducing expenditure.—We have in the foregoing paragraphs indicated the results of the evidence which has been placed before us upon the question whether the deficiency caused by exchange may be met by increase of taxation. There is, as has been already pointed out, another way in which a deficiency may be met, *viz.*, by reduction of expenditure. We are quite alive to the importance of this resource, and to the expediency of urging economy in every practicable way, more especially as there is no such pressure brought to bear on the Government of India as that to which the Chancellor of the Exchequer in this country is subjected by the representatives of the taxpayers. But, difficult as it is for us to form an opinion on the possibility of raising additional revenue, it is still more difficult to estimate the possibility of reducing expenditure. In order to do so, it would be necessary to enter upon an examination of the policy and action of the Government of India both in military and civil matters, a task which is beyond our province. Experience, however, shows as regards military expenditure that it is at all times difficult to resist its growth, and that occasionally the circumstances which call for it are beyond the control of any Government; while, as regards civil expenditure, advancing civilisation brings with it constantly increasing demands for Government action and enterprise—demands which are not the less urgent when, as is the case in India, they must originate with the Government rather than, as in Europe, with the people. Although, therefore, we feel strongly the necessity for the utmost care in restricting expenditure, we are certainly not in a position to conclude that any economies are possible which would enable the Indian Government to meet successfully the great and growing deficit caused by falling exchange.

46. Possibility of reducing deficit by charging more expenditure to capital.—It has been suggested that the Government of India might with propriety charge more of its public works expenditure to capital, and thereby reduce the deficit shown in the Revenue Account. On this point we can only say that the Government of India have for a long time acted on the sound principle of charging to capital only such outlay as is incurred for productive works, and that a policy of allowing unproductive expenditure to be so charged is obviously open to serious question.

Proposals of the Government of India.

47. Proposals of the Government of India. Despatch of 21st June 1892. Sir D. Barbour's Minute.—We have said enough to show that the situation is a very critical one, and the proposals of the Government of India are entitled to the most careful and anxious consideration. We proceed to state the

nature of those proposals. In a despatch of the 21st of June 1892, the Government of India expressed their deliberate opinion that if it became clear that the Brussels Conference was unlikely to arrive at a satisfactory conclusion, and if a direct agreement between India and the United States were found to be unattainable, the Government of India should at once close their mints to the free coinage of silver, and make arrangements for the introduction of a gold standard. The Government forwarded as an enclosure in this despatch a Minute by Sir David Barbour, the Financial Member of Council, giving an outline of the method he proposed for the introduction of a gold standard into India, if such a measure should become necessary. The nature of the plan will appear from the following extract from that Minute:

"6. The only measures for the introduction of a gold standard into India which seem to me feasible are the following:

"(1) The first measure would be the stoppage of the free coinage of silver. Government would retain the right of purchasing silver and coining it into rupees.

"(2) The next measure would be to open the mints to the free coinage of gold. Any man bringing gold to the mints would be entitled to have it coined into gold coins, which would be legal tender to any amount. It would be desirable to stop the free coinage of silver some time before opening the mints to the free coinage of gold. It would be a valuable guide to us in subsequent proceedings to know exactly what effect the stoppage of the free coinage of silver had on the gold value of the rupee.

"The new gold coins might be a 10-rupee piece and a 20-rupee piece.

"7. The weight and fineness of the gold coins to be issued from the mint would be such that the par of exchange between them and the sovereign would be the exchange which it was desired to establish between India and England.

"For example, if we wished the rupee to be worth 1s. 4d., the 10-rupee coin would contain as much gold as was worth (1s. 4d.) × 10 = 160 pence. The quantity of fine gold in the 10-rupee piece would be $\frac{160}{240}$ths, or two-thirds of the quantity contained in the sovereign.

"8. The question of the ratio at which we should exchange from the silver to the gold standard would require careful consideration.

"We ought not to think of going back to the old ratio of 1 to 15½. Neither ought we to adopt the very lowest price to which silver may have fallen at any time, or to consider ourselves bound to accept the market ratio of the very moment at which the change was made. A ratio based on the average price of silver during a limited period before the introduction of the gold standard would probably be both the safest and the most equitable"

48. Telegram of 22nd January 1893.—In a telegram of the 22nd of January 1893, the Government made this further statement regarding their proposals:

"We propose to take power to declare by notification that English gold coinage shall be legal tender in India at a rate of not less than 13½ rupees for one sovereign, and we have provided for that in the draft Bill. We think that an interval of time, the length of which cannot be determined beforehand, should elapse between closure of the mints and any attempt to coin gold here. The power to admit sovereigns as legal tender might be of use as

an *ad interim* measure, and need not be used except in case of necessity."

49. Draft Bill.—A copy of the draft Bill for the purpose of stopping free coinage was afterwards forwarded. It proposed to repeal the free coinage provisions of previous legislation, and to enact that the Governor General in Council might, by order notified in the *Gazette of India*, declare that any gold coins, which were for the time being a legal tender in England, should be a legal tender in India in payment or on account at such rate, not being less than $13\frac{1}{3}$ rupees for one sovereign, *i.e.*, at the rate of 1*s.* 6*d.* per rupee, and so for any greater or smaller coin, as should be fixed in such order, and might in like manner cancel or vary such orders.

50. Sir D. Barbour's arguments in support of the proposals.—In the Minute of Sir David Barbour forwarded by the Government of India, to which reference has already been made, the arguments in support of the proposals are stated. He observes that, although it is proposed to stop the free coinage of silver and to establish a gold standard, it is no part of the plan to substitute gold for silver as the ordinary currency of the country. It is contemplated that in the vast majority of Indian transactions silver would still be used as the medium of exchange. He refers to the example of France and other nations as showing that it is possible to have a gold standard, though a large percentage of the circulation consists of overvalued silver coins, which are legal tender to any amount. He concedes that, in order that the gold standard may be effective, a limit must be placed on the number of such coins, and they must be convertible into gold coins, either without payment of premium or on payment of a trifling premium, whenever any person wishes for gold coins in exchange for silver coins. Gold coins would only be required in exchange for silver when they were wanted for hoarding or export, or for melting down into ornaments. It is pointed out that one mode in which the scheme might be carried out would be by adopting measures for accumulating a store of gold, and, when sufficient had been obtained, opening the mints to the free coinage of gold coins, that metal being then made legal tender, and the exchangeability of silver for gold coins, according to their face value, guaranteed by means of the accumulated stock of gold. This, it is said, would be an expensive plan, and there would be a great risk of the whole stock of gold being drained away in exchange for silver rupees. Sir David Barbour, therefore, does not recommend this plan, but the measures which appear to him feasible are those described in the passage from his Minute already quoted. It is said that under the proposed scheme, if the Government treasuries were required to give gold coins for silver, whenever it was possible for them to do so, there could not be any considerable premium on gold coins so long as there were any in the public treasuries or in the Paper Currency reserve, and the gold standard would be effectively maintained. After the proposed measures had been carried out, it might happen that no gold was brought to the mints to be coined and to be put into circulation, and that the rupee

fell in value below 1*s.* 4*d.*,—supposing that to have been the ratio fixed,—or it might happen that, though gold was brought to the mints for a time and the rupee was worth 1*s.* 4*d.*, yet subsequently gold ceased to be brought to the mints, gold coins ceased to be found in circulation, and the rupee fell below 1*s.* 4*d.* In either case it would be a sign that the rupee was redundant, or, in other words, that there were too many silver rupees in circulation, and consequently their value had fallen below sixteen pence each, and that the gold standard was no longer effectively maintained. The remedy in such a case, it is said, would be to contract the rupee currency, and to adopt any feasible measures for improving the general financial position of the country. Such an improvement would give increased confidence, and the reduction of the rupee currency, if carried far enough, must ultimately restore the value of that coin. The greatest danger, it is said, would arise immediately after the first introduction of the gold standard, and would be brought about by silver rupees being, as they certainly would be, returned to India from foreign countries, and by their being thrown into the active circulation from Indian hoards. It is thought, however, that the existing hoards in India would practically remain unaffected. The reduction of the rupee currency, it is said, might or might not prove a very expensive measure. It could be spread over a number of years, and, until it had been carried out to a sufficient extent, the gold standard would not be effectively maintained. Of course, while the reduction of the rupee currency was in progress, there would not be an effective gold standard; but even during that period of uncertainty it might be expected that the exchange with England would remain much steadier than it had been during the last few years.

Effect of the proposals.

51. Substance of the proposals.—We proceed now to consider the proposal of the Government of India to close the mints, in the first instance, without adopting a gold standard, but coupled with the provision that the Indian Government should have the power of declaring English gold coins to be legal tender in India at a rate to be fixed by proclamation, such that the value of the rupee so fixed shall not exceed 1*s.* 6*d.*

52. Effect of closing the mints on uncoined silver.—Let us consider what would be the immediate effect of these proposals. First, then, as to their effect on the gold value of uncoined silver, and on the future relation of uncoined silver to the coined rupee.

53. Minting of silver would for the time be at an end, and this use of or demand for uncoined silver would cease to exist. What has been the use or demand? and what would it be likely to be in the future? Some notion may be formed on this point by examining the quantity of rupees coined in the last few years and of silver deposited in the currency reserves against the issue of notes.

54. Amount of new coinage in India in recent years.—The average amount of the new coinage in India has been as follows:—

	Rx.
(Annual average)—	
1870-71—1874-75	2,931,282
1875-76—1879-80	8,493,881
1880-81—1884-85	4,480,408
1885-86—1889-90	8,310,788
(One year)—	
1890-91	13,163,474
1891-92	5,553,970
1892-93	12,705,210
Yearly average—	
1870-71—1892-93	6,630,628
1875-76—1892-93	7,658,223

55. Silver bullion in Paper Currency reserve.—The annual average of silver bullion in the Paper Currency reserve has been as follows:—

	Rx.
(Annual average)—	
1870-71—1874-75	1,468,771
1875-76—1879-80	1,319,060
1880-81—1884-85	756,894
1885-86—1889-90	1,019,828
(One year)—	
1890-91	747,974
On the 31st of March 1892 it was	1,775,569
The average for the 22 years being	1,152,105

56. Total demand of India for currency purposes.—Looking to these figures, it will be seen that the absorption by India of silver for currency purposes since 1875 has averaged more than Rx. 7,700,000 a year. The coinage from 1885-86 to 1892-93 was Rx. 72,976,594, making an annual average of about Rx. 9,122,000. This is equivalent to 34,200,000 ounces of silver.

57. Imports of silver into India.—The net imports of silver into India have been as follows:—

	Rx.
(Annual average)—	
1870-71—1874-75	3,063,082
1875-76—1879-80	7,054,200
1880-81—1884-85	6,080,527
1885-86—1889-90	9,635,134
(One year)—	
1890-91	14,175,136
1891-92	9,022,184
1892-93	12,863,569

	Rx.
Yearly average—	
1870-71—1892-93	7,183,722
1875-76—1892-93	8,328,344

So that nearly the whole of the silver imported into India has been absorbed by currency demands, or has passed through the mints.

58. **United States currency demand.**—The United States currency demand is 54,000,000 ounces of silver a year.

59. **Production of silver in the world.**—The production of silver in the world is estimated for 1892 to have been from 152,102,000 to 157,535,000 ounces.

60. **Probable consequence of cessation of American and Indian demands.**—The currency demands of India, therefore, have during recent years been nearly a quarter, and those of the United States rather more than a third, of the whole world's production. If, therefore, either the one or the other were to cease, there ought, according to general laws, to be a great fall in the value of silver; and, if both were to cease, the fall ought to be very great indeed until the reduction of the demand had produced a similar effect on the supply. We have already explained that this reduction in supply might not follow for some time the diminution of demand, and the fall might be protracted for a long time.

61. **Possible panic.**—No safe inference, however, as to the effect of the cessation of the Indian or American demand can be founded exclusively on these figures. Apprehension of the future often operates on the minds of men, and produces an effect on the market greater than the actual circumstances of demand and supply would seem to warrant. The closing of the Indian mints would, no doubt, make it more likely that the United States would give up buying silver; and, if the apprehension of this were added to the cessation of the Indian demand, the effect might be a panic in the silver market. Eventually the price of silver would, no doubt, settle down to the new circumstances of demand and supply.

62. **Possible rise in value of gold.**—There is still another element to be considered. If the effect of the proposal of the Indian Government were sooner or later to cause a demand for gold in India which does not exist, it might raise the value of gold as against all other things, including silver. In other words, the gold price of silver might be still further diminished.

63. **Effect on value of uncoined silver.**—All the factors of the problem are so uncertain that it is impossible to predict with any confidence or in numerical terms what the effect of closing the mints would be on the value of uncoined silver. The greater the effect, the greater, of course, would be the difference in value between coined and uncoined silver in India, and the greater the dangers, whatever they may be, which might arise from that source.

64. **Effect on value of coined rupees.**—Next, as to the effect of simply closing the mints on the future value or gold price

of the rupee. If there be already, as there is reason to suppose, a quantity of unused rupees in India, they would have to be absorbed before the closing of the mints produced an effect on the value of the rupee. In that case, there might be some time to wait before there was any increase in its value. The apprehensions of men concerning the future might cause an immediate effect of a serious character; but we cannot venture to say for what length of time this would be maintained. Neither could we trace the progress of the enhancement of the value of the rupee in respect of time or place which we should expect to follow the closing of the mints.

65. Effect of closing the mints, coupled with making the sovereign a legal tender at 1*s*. 6*d*. the rupee.—It is impossible to estimate the extent to which the rupee might be raised if the Indian mints and Indian currency were to remain closed against both precious metals. The Government of India, however, add the proposal to make English sovereigns legal tender at a ratio which is not to exceed 1*s*. 6*d*. to the rupee; and it remains to be considered what would be the effect of stopping the free coinage of silver taken in conjunction with this condition. The proposal would leave it in the discretion of the Indian Government either to fix that ratio at once or to proceed by successive stages. If the higher ratio were adopted, if the Government were not itself to add rupees to the currency, and if in consequence of the closing of the mints exchange rose rapidly to that ratio, the difficulties and evils arising from an appreciation of the currency, to which we shall have to call attention hereafter, would be so much the greater; if a lower ratio were adopted in the first instance, and if exchange were to rise more gradually, these difficulties and evils would be less; but, whichever plan were selected, the Indian Government would probably be deemed by the public to have decided that 18*d*. was to be the gold value of the rupee, which consequently would be regarded as a limit. When that limit was reached, the currency would again become automatic, since gold sovereigns could be freely exported to India to serve as currency there.

Objections to the proposals: (1) *as to their practicability.*

66. Practicability of maintaining the rupee at an artificial value. Precedents.—The first objection taken to the scheme of the Indian Government is that it would not be practicable to maintain the rupee in the manner suggested on a ratio to gold much higher than that of the intrinsic value of the silver of which it consists. We have already alluded to the reliance placed by the Government of India upon the phenomena exhibited in the currency system of France and other nations. It will be important, therefore to direct attention to the essential features of the present Indian currency, and to consider what light is thrown upon the proposals of the Government of India by the experience derived from the currency arrangements of other countries.

Different Currency Systems of different Nations.

1.—*United Kingdom.*

67. Principles of currency of United Kingdom.—The present Indian monetary system is substantially modelled on that of the United Kingdom, the essential features of which are—

(1) The standard coin to be of one metal, gold.

(2) The mint to be open to the free coinage of this metal, so that the quantity of current coin shall be regulated automatically, and not be dependent on the action of the Government.

(3) Token coinage to be of a different metal or metals, subsidiary to the standard coin, legal tender only to a limited amount, and its face value and the price in the standard metal at which it can be obtained from the mint being greater than the market value of the metal contained in it.

It may be added that, under the Act of 1844, paper money is convertible on demand into gold, its quantity above a fixed amount varying with the quantity of gold against which it is issued.

68. Gold formerly considered the principal medium of exchange.—Lord Liverpool and other authorities would have added that the standard metal, gold, should be the principal medium of exchange; but this is no longer the fact. Gold is the standard or measure, but for the most part not the medium itself. Though, however, in wholesale transactions, and in a great many retail purchases, gold is no longer the medium of exchange, the use of gold coins is probably greater in the United Kingdom than in most other countries.

69. As regards the stocks of gold and silver (other than mere token money) in the United Kingdom and in India, such information as we have been able to obtain leads to the conclusions contained in the two following paragraphs.

70. Stocks of legal tender money in the United Kingdom.—In the United Kingdom the amount of gold and silver available for the purposes of currency is uncertain; but the Mint estimate of the gold in circulation is 91,000,000*l*., of which the amount in banks (including that in the Issue Department of the Bank of England and in other banks against which notes are issued) is stated to be 25,000,000*l*.

There is also the fiduciary issue of notes by the Bank of England and other banks, which at the close of 1892 stood at 27,450,000*l*.

It must, however, be remembered that the gold held by the Issue Department of the Bank of England and the gold held by the Scotch and Irish Banks in respect of notes issued beyond the authorised limits cannot be looked up as an integral portion of the currency, since it cannot be used at the same time with the notes which are

issued against it; but the amount is included in the sum of 21,000,000*l.* above mentioned in order to facilitate comparison with foreign countries which keep a gold reserve against their notes though not under conditions so strict and specific as those of the English Act of 1844.

India.

71. Principles of currency in India; stock of silver. —In the Indian currency system, as established in 1835, silver takes the place which gold occupies in the English system. Cheques, bankers' money, and other credit have not in India replaced the metallic currency to the same extent as has been the case in England.

The Indian Mint is open to the free coinage of silver; the rupee and the half-rupee are the only standard coins, and are legal tender to an unlimited amount. It is uncertain what is the stock of rupees in India, but it must be very large; Sir David Barbour says that the amount in active circulation, in which, of course, the hoards are not included, has been recently estimated at Rx. 115,000,000; and by some writers it has been placed much higher. Mr. F. C. Harrison, who has taken great pains in the investigation, puts it at Rx. 134,170,000, besides Rx. 30,000,000 of the coins of Native States.

Gold is not legal tender, and there are no current gold coins.

There is a subsidiary silver fractional coinage, which is legal tender only to the limit of one rupee.

Paper money may be issued to the amount of 8,00,00,000 rupees against securities; and beyond this only against a reserve of coin or bullion deposited. The amount of notes so issued was Rs. 26,40,18,200 on the 31st of March 1893, and the reserve was constituted as follows:—

	Rs.
Coin	17,53,85,744
Bullion	86,82,456
Securities	8,00,00,000

For the purposes of the Paper Currency India is divided into circles, at present eight in number. The notes are legal tender for five rupees and upwards within the circle for which they are issued, and are convertible at the office of issue, and (except in the case of British Burma) at the principal city of the Presidency to which the circles of issue belongs.

72. Other countries: principles of currency and stocks.—When we proceed to examine the currencies of other countries, we find that many of the conditions which have been considered essential in the English and Indian currencies are either wanting altogether or have been replaced by other conditions. The following is a short statement of the most important features in

these currencies, and of the stock of gold, silver, and notes available for currency, so far as we have been able to obtain them, as they stood at the close of 1892; but we must guard ourselves against being supposed implicitly to accept all the figures.

United States.

73. United States.—The standard is gold and the mint is open to gold.

There is little gold coin in circulation, at any rate in the Eastern States, but a large reserve of gold in the banks and in the treasury—

	£
Stock in the Banks	82,250,440
Stock in the Treasury	48,852,290
Silver dollars in the Treasury	70,948,080
Silver dollars in circulations	12,334,490

and these, or the certificates issued against them, circulate at a gold value at the old ratio of 16 to 1.

There was also in the Treasury of silver bullion an amount valued at 17,874,430*l*., against which paper certificates are issued, which circulate at a gold value at the same ratio.

The aggregate paper currency was about 210,000,000*l*.

The silver currency and paper based on silver are accepted as legal tender to any amount, and there is no premium on the gold and gold certificates in comparison with them.

74. Silver maintained at ratio of 16 to 1.—In this case a very large amount of silver, or certificates representing such silver, has hitherto been kept in circulation at the ratio of 16 to 1. But there is considerable apprehension concerning the difficulties which may arise if the compulsory purchase of silver by the Treasury for currency purposes should continue. Under the Bland Act passed in 1878 these purchases amounted, as above stated, to about 20,600,000 ounces in the year, whilst under the Sherman Act, which was passed in 1890, these purchases have been increased to an annual amount of 54,000,000 ounces.

Canada.

75. Canada.—The standard is gold; but though there is a provision for coining gold dollars at the rate of $4 \cdot 86\frac{2}{3}$ to the British sovereign, that is, at the ratio of 16 to 1, there is no Canadian gold coin, and little or no gold coin in circulation.

Canada has no mint. Fractional silver currency is supplied from England.

The stock of gold is said to be about 2,400,000*l*.

There are about 3,700,000*l*. worth of Dominion notes of various amounts from 25 cents up to 4 dollars; and the banks may issue notes for 5 dollars or any multiple thereof to an amount not exceed-

ing their "unimpaired paid-up capital," such notes being redeemable in specie or Dominion notes; the present issue is about 7,000,000*l*.

The Dominion notes (unless it be for small amounts) are redeemable in "coin current by law in Canada," that is, in such dollars as above mentioned. The American silver dollar circulates at par at the ratio of 16 to 1, although a Government proclamation was issued in 1870 declaring it to be legal tender up to the amount of 10 dollars, but only at 80 cents per dollar.

Silver is not convertible into gold.

76. Notes and silver at gold value of United States.—This is a very remarkable case, since without any gold currency, and without even a mint for gold, dollar notes and silver dollars circulate at the United States gold dollar value.

West Indies.

77. West Indies.—All the West India Islands and British Guiana have adopted the English currency, gold being the standard, but silver being a legal tender without limit. In practice, British gold is never seen there, but the circulating medium consists of shillings and Colonial bank notes. Except in British Honduras, no silver dollars are legal tender, but gold doubloons remain legal tender at 64 shillings (the rate fixed in 1838) throughout the West Indies.

In Jamaica and Trinidad gold doubloons and United States gold coins are not uncommonly seen; they come from the Isthmus and Venezuela, and go to New Orleans and New York in a steady current.

In the Bahamas the United States gold dollar (worth 4*s*. 1·316*d*.) is popularly over-rated at 4*s*. 2*d*., and consequently American eagles circulate freely (or did so until notes were introduced).

British Honduras has as its standard the silver dollar of Guatemala, which is a 5-franc piece without any gold behind it.

78. Silver token currency at gold value.—This is an instance of a gold standard without gold and a silver token currency circulating to an unlimited extent at a value based on that gold standard.

Germany.

79. Germany.—Germany in adopting a gold standard in 1873 adopted most of the features of the English currency system. The mint was opened to gold, and a subsidiary silver token coinage was introduced, limited in quantity by reference to population, and legal tender only to a limited amount. The peculiarity of the case of Germany is that 20,000,000*l*. worth of old silver thalers are retained in circulation at a ratio of 15½ to 1, and are legal tender to an unlimited extent. Of the new coinage of gold, the banks hold

34,250,000*l*., in addition to 6,000,000*l*. stored at the fortress of Spandau, while the amount in circulation is estimated to be from 65,000,000*l*. to 70,000,000*l*.

The amount of paper currency issued is 6,000,000*l*. by the Imperial Government, 53,790,000*l*. by the Reichsbank, and 8,950,000*l*. by other banks, making a total of 68,740,000*l*.

80. Resembles that of United Kingdom.—On the whole, the German system approximates more closely than any other to our own, though it is said that there are not equal facilities for obtaining gold for export.

Scandinavia.

81. Scandinavia.—The standard has been gold since 1873, and the mints appear to be open to gold, but there is little gold in circulation. Bank-notes convertible into gold are the ordinary currency.

Silver is only subsidiary token currency. The stock of gold held by the banks appears to be about 5,500,000*l*., and of notes about 13,000,000*l*.

The Latin Union.

(*a*) *France.*

82. Latin Union. France.—The mints are open to gold.

Silver coinage, except of subsidiary coins, has since 1878 been, and is now, prohibited under the rules of the Latin Union.

There is a large quantity of gold coin in actual circulation.

The peculiarity of the French currency is the large amount of 5-franc pieces which circulate at the old ratio of 15½ to 1. They are legal tender to any amount, and are accepted as freely as the gold coin. They are not legally convertible into gold.

The stock of currency appears to be as follows:—

	£
Gold, about	171,000,000
Silver	140,000,000
Notes	132,000,000

The notes of the Bank of France are convertible into gold or silver, at the option of the bank. The bank pays gold freely for home use; but, if gold is required in large quantities, especially for exportation, special arrangements must be made.

There is no difficulty in maintaining either the silver or the notes at their gold value.

83. Gold standard, with much silver circulating at gold value.—Here is a currency which for all practical purposes appears to be perfectly sound and satisfactory, but which differs from our own in most important particulars. It is sometimes called

"étalon boiteux," or limping standard; but, inasmuch as the mint is open to gold and closed to silver, the standard is really gold, whilst a very large proportion of the currency is either inconvertible silver, or notes payable (at the option of the bank) in silver or gold, maintained without difficulty at the above-mentioned artificial ratio.

(b) Belgium.

84. **Belgium.**—The mint is open to gold.

The rules as to 5-franc pieces as to the ratio between gold and silver and as to legal tender are the same as in France.

The stock of currency appears to be as follows:—

	£
Gold, about	5,000,000 or more
Silver, 5-franc	8,000,000
Notes	15,000,000

The notes appear to be convertible into either gold or silver, at the option of the bank.

85. The situation is the same as in France; but inconvenience might be experienced if the Latin Union were to be terminated, and the several members were obliged, under the conditions imposed by that Union, to liquidate in gold their silver currency held by France.

(c) Italy.

86. **Italy.**—The mint is open to gold.

The rules as to 5-franc pieces as to the ratio between gold and silver and as to legal tender are the same as in France.

The stock of currency appears to be—

	£
Gold	23,600,000
Silver, 5-franc pieces	4,000,000
Notes	57,000,000

There is very little metallic coin in actual circulation; the paper is at a discount, and the exchange below par.

87. The state of this currency is unsatisfactory—not, however, on account of the artificial ratio between gold and silver, but on account of the want of both metals—owing probably to the state of the finances and credit of the country. The same difficulty would arise as in Belgium if the Latin Union were terminated.

Holland and the Dutch East Indies.

88. **Holland and the Dutch East Indies: History of adoption of gold standard.**—From 1847 to 1873 Holland and its dependencies had the single silver standard. In consequence of the changes in Germany and other countries in the north of

Europe, which adopted the gold standard in 1873, Holland suspended the coinage of silver in that year. Silver could no longer be brought to the Dutch mint, and gold coin could not be issued, because the Dutch Parliament had not agreed on a gold coin or a gold standard. There was a certain quantity of silver coins in circulation, and their value at this period was regulated neither by the market value of gold nor by that of silver. The demand for coin was increasing in the years 1873 to 1875; and the result was that, whilst the value of silver as a metal was going down in the market, Dutch silver coins were appreciated as against gold. The rate of exchange on London, which oscillates now on the gold basis between 12·1 and 12·3 florins to the £ sterling, shrank to 11·12 florins.

In 1875 the gold standard was adopted at a ratio of 15⅝ths to 1, and the Dutch mint was opened to gold; whilst the coinage of silver, except of subsidiary token coins, was prohibited, and remains so at the present time. A considerable quantity of gold coin was minted, which was, however, kept in reserve, and not used for internal circulation. Silver florins at the gold value were legal tender to any amount; and, with paper florin notes, which were also at a gold value, formed the internal circulation of the country. Neither silver nor paper is convertible into gold; but the Netherlands Bank has always been willing to give gold for exportation. In 1881 and 1882 the balance of trade turned against Holland, and the stock of gold ran down to about 600,000*l*. Under these circumstances, an Act was passed in April 1884, which enabled the Government to authorise the bank to sell at market prices a quantity of 25,000,000 silver florins, whenever the state of the currency might demand it. This Act has never been brought into operation, but it has restored confidence; the necessary stock of gold, amounting now to upwards of 5,000,000*l*., has been maintained; the Bank gives gold freely for export; and the exchange has continued steady at from 12·1 to 12·3 florins to the £ sterling. No difficulty has been experienced either in Holland or in her Eastern dependencies. The system of currency has always been, and still is, the same in both. There is no mint and little or no stock of gold in Java; and at the same time the rate of exchange between Java and Europe is always at or about par. It should be added that Java merchants can always do their business with gold countries through Holland.

The stock of currency is as follows:—

	In Holland	In Java
	£	£
Gold, about	5,200,000	500,000
Silver	11,000,000	2,773,000
Paper	16,000,000	4,250,000

89. Gold standard, with silver and paper currency.—This is a case in which the standard is gold, with little or no

gold in circulation. The silver is kept at an artificial ratio much higher than its market value, although neither it nor the paper is convertible into gold except for purposes of export. This artificial exchange is maintained in the Dutch East Indies, where there is little or no gold, as well as in Holland, where there is a limited stock.

Austria-Hungary.

90. Austria-Hungary: History of adoption of gold standard.—Before 1879 the standard coin was the florin, which was equal to $\frac{1}{45}$ th part of a pound of fine silver. The mint was open to silver, and silver florins and silver florin notes were legal tender to an unlimited amount. The actual circulation consisted of florin notes, which were inconvertible; their amount was 52,500,000*l.* in 1879 and 69,500,000*l.* at the beginning of 1892. The average exchange on London for 10*l.* sterling was 141·78 in 1861* after the Italian war. It became 109 in 1865, but rose to 125·98 in 1867 after the Austro-Prussian war. It fell to 110·53 in 1872, continued

* Table given by M. Soetbeer (*see* Appendix to Gold and Silver Commission's Report, page 209), which differs slightly from the figures of exchange on London given below, which have been furnished by the Anglo-Austrian Bank.

Year.	Annual average of exchange on London in Vienna.	Average price of Bar Silver per ounce in London. (Pixley & Abell.)
		d.
1873	110·89	$59\frac{1}{4}$
1874	110·91	$58\frac{5}{16}$
1875	111·78	$56\frac{7}{8}$
1876	121·32	$52\frac{3}{4}$
1877	122·17	$54\frac{13}{16}$
1878	118·99	$52\frac{9}{16}$
1879	117·30	$51\frac{1}{4}$
1880	117·83	$52\frac{1}{4}$
1881	117·83	$51\frac{11}{16}$
1882	119·60	$51\frac{5}{8}$
1883	120·00	$50\frac{9}{16}$
1884	121·89	$50\frac{5}{8}$
1885	124·92	$48\frac{5}{8}$
1886	126·01	$45\frac{3}{8}$
1887	126·61	$44\frac{5}{8}$
1888	124·22	$42\frac{7}{8}$
1889	119·55	$42\frac{11}{16}$
1890	116·05	$47\frac{11}{16}$
1891	116·80	$45\frac{1}{16}$
1892	119·29	$39\frac{13}{16}$

at 111 till 1875, but rose to 122·25 in 1877, 117·89 in 1878, and 116·63 in 1879. It seems that in the earlier years there had been a premium on silver, the paper money being depreciated below its face value, so that no silver was brought to be coined. But silver fell in price from 59¼*d*. per oz. in 1873 to 51¼*d*. per oz. in 1879; the notes ceased to be depreciated; and as the Austrian mint was open to silver, it became worth while to bring silver to the mint to be coined; so that, between August 1878 and November 1879, the silver circulation had increased by 7,000,000*l*. Under these circumstances, the Austro-Hungarian Government in March 1879 stopped the coinage of silver on private account, but continued coining it at their own discretion. The quantity so coined between 1880 and 1891 appears to have amounted to 125½ millions of florins. This state of things continued till 1891, when the Austro-Hungarian Government determined to propose the adoption of a gold standard and to open the mint to gold, for which the necessary measures were passed by the Austrian and Hungarian Legislatures in August 1892. From 1879, when the mints were closed against the private coinage of silver, the average exchange for 10*l*. sterling rose from 117·83 florins in 1880 and 1881 to 126·61 florins in 1887, and then fell to 116·80 in 1891 and 119·29 in 1892. The whole oscillation between 1879, when the mints were closed, down to 1891, when the resolution to adopt a gold standard was taken, was less than 9 per cent., and at the end of the period it stood at nearly the same figure as at the beginning, though in the meantime the price of silver had fallen by nearly 12 per cent., and in 1891 it was more than 6*d*. per oz. lower than in 1879. The basis for conversion to a gold standard, which appears to have been founded on an average of this exchange, is a ratio of 18·22 silver to 1 gold, or 1 gold florin = 2 francs 10 centimes, making 120·1 florins equal to 10*l*. The mint is now open to gold.

The Austrian Government have now at their command a reserve of about 351,000,000 florins (or nearly 30,000,000*l*.) in gold, and it appears to be intended that a certain quantity of paper and of silver florins shall be withdrawn from circulation, and that the paper florins remaining in circulation shall be convertible into gold.

91. Parity of exchange maintained by closing mints.—This is a very remarkable case. The fall in exchange, which would have accompanied or followed the fall in the market value of silver, has been averted by closing the mints against free coinage of silver. Fair steadiness of exchange has been maintained for more than a decade, although the paper currency was inconvertible, and silver was coined on Government account alone; and in the end a law has been passed for the adoption of a gold standard, a gold reserve has been accumulated, and the mint has been opened to gold.

A fractional subsidiary coinage of silver is provided for, but the currency will probably consist in the main of paper notes convertible into gold.

Brazil.

92. Brazil. Parity of forced paper currency maintained.—The case of Brazil is perhaps the most remarkable of all, as showing that a paper currency without a metallic basis may, if the credit of the country is good, be maintained at a high and fairly steady exchange, although it is absolutely inconvertible and has been increased by the act of the Government out of all proportion to the growth of the population and of its foreign trade. The case, it need hardly be said, is not quoted as a precedent which it is desirable to follow.

The Brazilian standard coin is the milreis, the par gold value of which is 27*d.* A certain number were coined, but have long since left the country, and the currency is and has since 1864 been inconvertible paper. The inconvertible paper was more than doubled between 1865 and 1888, but the exchange was about the same at the two periods, and very little below the par of 27*d.* It had gone down to 14*d.* in 1868, the date of the war with Paraguay, but had risen again, and was in 1875 as high as 28$\frac{3}{8}$*d.* In 1869, when the quantity of paper money was increased from 12,468,000*l.* to 18,322,000*l.*, the mean rates of exchange showed an advance of about 11$\frac{3}{4}$ per cent. Since the revolution which displaced the Empire and established the Republic, the paper issues of the banks were increased by more than 30,000,000*l.* in less than three years, so that the paper issue in 1892 amounted to 51,372,700*l.*; and as the result of this, and of diminished credit, the exchange in that year ranged from 10$\frac{1}{4}$*d.* to 15$\frac{3}{4}$*d.*

Results of Examination of different systems of currency.

93. Parity of exchange maintained under various circumstances.—It is impossible thus to review foreign systems of currency without feeling that, however admirable may be the precautions of our own currency system, other nations have adopted different systems which appear to have worked without difficulty, and have enabled them to maintain for their respective currencies a gold standard and a substantial parity of exchange with the gold-using countries of the world, which has unfortunately not been the case with India. This has been effected under all the following conditions, *viz.*,—

(*a*) with little or no gold coin, as in Scandinavia, Holland, and Canada;

(*b*) without a mint or gold coinage, as in Canada and the Dutch East Indies;

(*c*) with a circulation consisting partly of gold, partly of overvalued and inconvertible silver, which is legal tender to an unlimited amount, as in France and other countries of the Latin Union, in the United States, and also in Germany, though there the proportion of overvalued silver is more limited, the mints in all these countries

being freely open to gold, but not to silver, and in some of them the silver coinage having ceased;

(*d*) with a system under which the banks part with gold freely for export, as in Holland, or refuse it for export, as in France;

(*e*) with mints closed against private coinage of both silver and gold, and with a currency of inconvertible paper, as has been temporarily the case in Austria;

(*f*) with a circulation based on gold, but consisting of token silver, which, however, is legal tender to an unlimited extent, as in the West Indies.

The case of Holland and Java is very remarkable, since in that case the gold standard has been maintained without difficulty in both countries, although there is no mint in the Dutch East Indies, no stock of gold there, and a moderate stock of gold in Holland; whilst the currency consists of silver and paper legally and practically inconvertible into gold, except for purposes of export. The case of Canada, which maintains a gold standard without a gold coinage, is also very remarkable.

94. Austria-Hungary compared with India.—The case of Austria-Hungary is also interesting, and presents a remarkable contrast to that of India, as will be seen from the following table:—

Year.	Average value of Florin deduced from the Table of Exchange on London in Vienna given at paragraph 88.	Average value of Rupee in London for Bills on India (for official years 1873-74, etc.)	Comparison of the two tables, taking the first year as equal to 100.	
	d.	*d.*	Austrian Florin.	Indian Rupee.
1873	21·64	22·35	100	100
1874	21·64	22·16	100	99·13
1875	21·47	21·63	99·21	96·76
1876	19·78	20·51	91·40	91·75
1877	19·64	20·79	90·76	93·02
1878	20·17	19·79	93·21	88·56
1879	20·46	19·96	94·55	89·31
1880	20·37	19·96	94·13	89·28

Year.	Average value of Florin deduced from the Table of Exchange on London in Vienna given at paragraph 88.	Average value of Rupee in London for Bills on India (for official years 1873-74, etc.)	Comparison of the two tables, taking the first year as equal to 100.	
	d.	d.	Austrian Florin.	Indian Rupee.
1881	20·37	19·89	94·13	89·0[illegible]
1882	20·07	19·52	92·74	87·36
1883	20·00	19·54	92·42	87·41
1884	19·69	19·31	90·99	86·39
1885	19·21	18·25	88·77	81·67
1886	19·05	17·44	88·03	78·03
1887	18·96	16·90	87·62	75·60
1888	19·32	16·38	89·28	73·28
1889	20·08	16·57	92·79	74·12
1890	20·68	18·09	95·56	80·93
1891	20·55	16·73	94·96	74·86
1892	20·12	14·98	92·98	67·04

It will be seen that a country with a silver standard, and a currency consisting partly of overvalued silver, but chiefly of inconvertible paper, has been able by closing its mints against private coinage for a series of years, and, whilst still continuing to coin silver on Government account, to maintain a fairly steady rate of exchange with gold-using countries for a considerable period preparatory to adopting a gold standard.

95. **Russia.**—Concerning the currency of Russia, we have less information than in the case of other countries. But it appears that there is little or no silver or gold coin in the country, and that the currency consists of inconvertible paper roubles based on silver. The Russian mint is now closed against the coinage of silver on private account. It is an interesting fact that the paper rouble, being in form a promise to pay silver, is now, owing to the fall in silver, exchanged for a higher value in gold than the silver which it promises to pay. Taking silver at 38*d.* per ounce, the silver rouble would be worth 23·774 pence, whilst the paper rouble is quoted at 25 pence. We have already called attention to a similar ex-

perience in the case of Austria-Hungary. The phenomenon can, of course, only arise when the amount of the paper currency is limited.

96. Result of the above precedents.—United States. France. Austria-Hungary.—It would thus appear that it has been found possible to introduce a gold standard without a gold circulation, without a large stock of gold currency, and even without legal convertibility of an existing silver currency into gold. Before concluding, however, that these precedents are directly applicable to the condition of things existing in India, it is necessary to examine them carefully. There is no one of the countries above referred to in which silver has been so largely and so exclusively used as in India during the last half-century; and in most of them the people have been for long accustomed to deal with their silver coins on the basis of a double standard. To the Frenchman 5-franc pieces, to the American dollars, have for generations been not only so much silver, but the equivalent of a certain quantity of gold; and it would have been a shock to his habits and mode of thinking to treat them otherwise. It may be easier to maintain an old and well-known silver currency at a gold value in countries which have been bimetallic, and in which large quantities of gold and silver are already in circulation, than to introduce such a system into a monometallic silver country such as India. The case of Austria-Hungary again differs from that of India in some important particulars. In Austria-Hungary the standard was silver with an inconvertible paper currency; and the state of this paper currency was probably one of the chief factors which made a fundamental change necessary. In making the change the relation of Austria-Hungary to the neighbouring countries was, no doubt, an important consideration, and the fact that Germany and other States had adopted a gold standard rendered it expedient to take a similar course.

97. Holland and her dependencies.—Even in the case of Holland and its East Indian Colonies, which is *primâ facie* very much in point, there are differences which detract from its value as a precedent for India. At the time the change of standard was adopted, the relative values of silver and gold had not parted as they have since done; and, as regards Java, it must be borne in mind that, although it is an Eastern country dealing largely with silver-using countries, it has always had the same standard and the same currency as Holland, the change being made in the standard of both at the same time.

98. General conclusion.—On the whole, it seems to us that, whilst the differences we have pointed out prevent the cases of the countries referred to from being applicable in all respects as precedents to the case of India, and the circumstances of each particular country must be studied, yet the experience derived from the currencies of those countries is not without value as bearing on the questions which we have to consider, and is important as showing under what various conditions the exchange value of a currency may be maintained.

Use of Precious Metals as Currency in India.

99. Question as to difficulty of getting the people of India to adopt gold.—It has been objected that the natives of India are accustomed to silver; that the transactions are small in amount, so that silver is better suited to their use than gold; and that they will not willingly give up the rupee. The answer to this is that it is not proposed to substitute the gold sovereign for the rupee as currency in ordinary use; and that the case would in this respect resemble that of many of the countries above referred to, where the standard is gold, but the ordinary currency is silver or paper.

100. Use of gold in India.—Moreover, gold has never been entirely out of use in India. It is true that in India silver has for the last 30 or 40 years been more exclusively used than in many of the countries referred to. But, though gold coins have not been in use as legal tender, and no fixed ratio has been established between gold and silver coins, there is no part of India in which gold coins are not well known and procurable, and recognised as a form of money, the value of the chief gold coins being regularly entered in the "Prices current." Until 1835 or thereabouts gold coins constituted a recognised part of the Indian currency, and they were received by the Government in payment of its demands till December 1852; and as late as 1854-55 gold coin to the value of 412,000*l.* was sent by the Government from India to London. The value of the gold imported into India in the eight years from 1862-63 to 1869-70 was no less than 50,000,000*l.*

101. Sir Charles Trevelyan, writing in 1864 in support of a proposal to make sovereigns legal tender in India, referred to the large importation of gold since 1860 as indicating "the determination of the people to have gold," and added that it "shows that the Government would be cordially seconded by them in any attempt to introduce a gold currency on a sound footing." The Secretary of State, Sir Charles Wood, when replying in the same year, wrote: "It is obvious from the information collected by Sir Charles Trevelyan that there is a very general desire for the introduction of gold coins in India," and "that the people, even in the upper and remote parts of India, are well acquainted with the sovereign." There is little question but that these observations are as applicable at the present time as when originally made.

102. The introduction of gold coins on an important scale would necessarily take place through the banks; and the complete success of the paper currency, as to the acceptance of which by the people of India there had been on the part of many persons serious doubts, shows that there need be no hesitation as to the introduction of a gold legal tender coinage on the ground of its novelty.

103. It may be added that the value of the net imports of gold into India since 1880 has amounted to more than Rx. 44,000,000; and it might be expected that much of the uncoined gold now in India, which must be very considerable, would be brought to the mints if a gold coinage were introduced on a proper basis.

Objections to the proposals: (2) on the ground of inexpediency.

104. Objections to the proposals on the ground of inexpediency.—So far we have been considering whether the proposals of the Government of India are practicable. We turn now to consider the objections taken to those proposals, even assuming that they would be effectual to maintain a stable exchange. Some of these objections are equally applicable, whether the exchange is or is not materially raised above its present level. Others are only of force on the assumption that exchange is to be so raised. We will deal first with those which are directed against the scheme generally on the assumption that the rate of exchange is not to be raised, but that a continued fall in the value of silver is likely to create a considerable divergence between the exchange value of the rupee and that of the silver of which it consists.

Objections—(a) Supposing the ratio not to be raised and silver to fall.

105. Spurious coinage.—It is anticipated by some that a serious amount of spurious coinage would result. If spurious coins to a large amount could be put in circulation, the transaction would no doubt be a profitable one; but in countries where silver coins having an intrinsic value much below their nominal value are in circulation, spurious coinage would be an extremely profitable enterprise, and experience shows that the apprehended danger has not been realised in these countries. Against this, however, it is maintained by some persons that this affords no guide as to what would be likely to happen in India, the natives of which country might, in their opinion, be expected to display great skill in the manufacture of spurious coins, while the people who receive them are guided more by the weight of metal in the coin than by its appearance. It is difficult to estimate with precision the real extent of the alleged danger, but when it is borne in mind that, in order to carry out operations on an extended scale, expensive and specially constructed machinery would be requisite, we doubt whether the danger of India being flooded with a large amount of spurious coin would really be a grave one.

106. Effect on hoards of silver.—The effect that, on the assumption with which we are now dealing, the closing of the mints would have upon the hoards of natives of India and upon their silver ornaments is more free from doubt. Coined rupees, of which it is said that the hoards chiefly consist, would be unaffected, except in so far as any further fall in their gold value would be prevented; but the uncoined silver and silver ornaments would cease to be convertible into rupees, and would certainly be depreciated in value. In times of scarcity and famine a considerable quantity of silver ornaments has found its way to the mints. During the period of the great famine in 1877 and the following years, for example, large quantities of such ornaments were minted. In three years no less than Rx. 4,500,000 were thus turned into money. It is said, however, that the transaction of converting silver ornaments

or hoarded silver into money is not at the present time effected by the owner himself taking them or sending them to the mints for conversion into rupees: it is through the intervention of the village money-lender that the transaction is carried out. Uncoined silver would, it is asserted, still be converted into money in the same fashion. This is, no doubt, true, but it is obvious that the ornaments would not be converted on terms as favourable to the seller. It cannot, we think, be doubted that the closing of the mints would in this case depreciate the silver ornaments and the uncoined silver hoarded by the people of India. Such a use of ornaments is, however, said to be rare.

107. Existing losses would be stereotyped.—A further objection is to the effect that the proposal of the Government of India would perpetuate the burden hitherto experienced by India owing to the fall of exchange, and that it would be unfair to stereotype the loss of persons entitled to be paid in rupees, and to deprive them by the act of the Government of the chance of a rise. To this it may be answered that having regard to the future prospects of the silver market, so far as they can be gauged at the present time, all persons concerned would probably be glad to lose their chance of a future rise on the terms of being secured against the effects of a fall.

108 Inconvertible token currency would be created with a gold standard, but without a gold currency.—Another objection is that the proposal of the Indian Government will, if there should in future be a divergence between the value of the rupee and the market price of silver, have the effect of converting the whole of the currency of India into a token currency, which would in no way differ in principle from an inconvertible paper currency. It must, however, be remembered that, although a nation possessed of a fairly satisfactory monetary system might well hesitate to exchange it even temporarily for an inconvertible currency, yet India already labours under difficulties the gravity of which is admitted. One of the greatest risks connected with an inconvertible paper currency is the temptation which it affords to the Government unduly to expand the amount in circulation; the proposal of the Indian Government, however, does not involve this danger. It is to be observed, too, that in the United States, in Germany, in the Latin Union, and in Holland a very large amount of silver coins has, with mints closed against the free coinage of silver, been maintained as full legal tender at a gold value far exceeding that of the silver they contain; whilst in Austria-Hungary during the recent fall in silver a forced paper currency, founded originally on that metal, has in exchange more nearly corresponded with the original gold value of the silver on which it was based than has the silver itself.

109. Currency would not be automatic.—Again, strong objections are urged to the power being placed in the hands of the Government to close the mints to the public, while retaining to itself the power to coin rupees, and thus to its being enabled at

will to contract or expand the currency. But the assumption we are now making is that the exchange is not to be materially raised above its present level. If the rise were checked by the reception of gold, as suggested by the Government of India, the discretionary power vested in that Government would be confined within very narrow limits, because, if the rupee were to rise above the fixed ratio to such an extent as to cover the expenses of transmission and of coinage, it would become profitable to take gold to the Indian mint or to send sovereigns to India, and thus the currency would be rendered automatic on a gold basis.

110. Burden of taxation would be increased.—It is further objected to the proposals of the Indian Government that they would make the value of the rupee greater than it otherwise would be, and that thereby the burden of Indian taxation would be increased. That part of the revenue which consists of fixed payments would remain unaltered in nominal value, whilst each rupee which the ryot pays would be worth more, and the rupee prices of the goods he produces would be less, than they would be if silver continued to fall. The argument is no doubt sound; but there are answers to this objection which have no little weight.

111. Present prices would not be altered.—Whether silver is falling or gold rising in value, or both movements are taking place, and whether an appreciating or a depreciating standard is the less open to objection, are questions of great difficulty. We are dealing with the assumption that the present ratio, or some ratio differing but little from it, is maintained. On the assumption the present level of rupee prices would not be at once altered; and if in future rupee prices became less and the burden of existing fixed taxation became heavier than they would have been if a silver standard had been maintained, this result would not be arbitrarily produced by the action of the Government, but would be due to the fact that the new standard was depreciating less or appreciating more than that for which it was substituted.

112. Alternative of increased taxation a still more formidable difficulty.—In the next place, it must be borne in mind that the alteration in the relative values of gold and silver has so increased the liabilities of the Indian Government in comparison with its revenues as to make it necessary, in the absence of other remedies, to impose fresh taxation. The evidence we have had from men whose experience qualifies them to judge points distinctly to the conclusion that, supposing the choice to be between an indirect increase of taxation arising from arrest of the fall in the value of the rupee, or even from a considerable increase in its value on the one hand, and the imposition of new taxation on the other, the latter of these courses would be far more likely to lead to popular discontent and political difficulty than the former.

113. Trade with silver-using countries.—The proposal of the Government of India in so far as it rendered the exchange between India and gold-using countries stable would introduce into the trade of India with silver-using countries the same disquieting

influences which, it is alleged, at present hamper the trade of India with gold-using countries. It must, however, be observed that the trade of India with silver-using countries only amounts to about half of her trade with gold-using countries.

114. Trade of India in competition with silver-using countries.—Another objection strongly urged is that if the proposal of the Government were carried out, and there should arise a great divergence between the ratio borne to gold by the rupee and by silver respectively, this would seriously affect the trade of India with silver-using countries, and stimulate in those countries the production of commodities which compete with Indian commodities in the markets of the world, and that the effect of such increased competition would be seriously felt by India.

115. Exports of India to silver-using countries.—To deal first with the point as it affects the trade between India and the silver-using countries which now take her commodities. The most important of these is China, which now takes from India a large quantity of manufactured cotton goods. China, it is said, would not give more silver for these cotton goods than it did before; but if the divergence between silver and the rupee were considerable, the same silver price would mean a lower rupee price. It is true this lower rupee price might represent a greater purchasing power than if the rupee had been allowed to fall *pari passu* with silver; but the manufacturer, it is contended, would find a difficulty in diminishing the rupee cost of production. Some of his expenses would consist of fixed payments, and the difficulty of diminishing the number of rupees paid in wages would be considerable. In the result, the trade would be less profitable, and its volume would be diminished. The reply made to this argument is that the Indian produce imported into China is paid for ultimately by goods exported by China to other countries, and that if the gold price of these commodities does not fall owing to a fall in the gold value of silver, they would realise a higher silver price, and that China would thus be able to pay a higher price for the Indian imports. We have already given our reasons for doubting whether the fall in the gold value of silver does operate to any considerable extent in reducing the gold price of commodities exported from silver-using countries.

116. Manufacture in such countries of goods competing with Indian exports.—It is suggested further that if the fall of silver should continue to be considerable, it would afford a great inducement to promote the manufacture in China of cotton goods in substitution for those now imported from India, and stress is laid upon the fact that the production of cotton goods in Japan has already become considerable. To this it is answered that China is slow to move, and that the impediments and burdens which are imposed upon industrial enterprise in China are such as to render the fear that the suggested change in the currency system of India would greatly stimulate the production of cotton goods in China unreasonable. Fears have been also expressed lest the production of cotton goods in Japan, where there is practically a silver

standard, should be further increased in consequence of the advantage which that country would gain by the fall in the value of silver as compared with India if the exchange there remained stationary. As to this argument we may refer to the remarks in paragraph 27, in which we have expressed our view that the stimulus thus caused to the export trade of a country can only be transitory, and can continue only until circumstances have brought about the inevitable adjustment. In the same paragraph we examined the trade statistics of India, and could not see any evidence that a relation existed between a fall in exchange and the volume of exports.

117. Opium trade with China.—It is, moreover, objected, and for the same reasons, that the opium trade between India and China would be seriously affected if the currency proposals of the Government came into operation, and that India must be content to receive fewer rupees for the opium exported to China. The average annual value of opium so exported is about Rx. 10,000,000, and the greater part of the decrease in its export value, supposing such decrease were realised, would fall upon the Government. It is obvious that in that event the effect upon the revenue would be very serious. In the case of opium, as well as cotton goods, it is argued that there would be a tendency to replace to some extent the use of Indian opium by opium grown in China. The same answer which has been given to this argument in relation to the trade in cotton goods is equally applicable with regard to the opium traffic. It must be remembered, too, that the production of opium in China is at the present time very large. The amount imported from India forms only a small portion of the total consumption. Indian opium is in truth a luxury; its use in preference to Chinese opium is a matter of taste, and depends upon its real or assumed superior qualities. Under these circumstances, it may be doubted whether any considerable diminution in the rupee value of opium exports to China would be likely to result from the adoption of the proposals of the Indian Government.

118. Competition of silver-using countries with India in other markets.—Those who object that the trade of India with other silver-using countries would be diminished in volume and profit by the adoption of the Government proposals lay, perhaps, even greater stress upon the advantage which a great divergence between silver and the rupee would give to those countries in their competition with India. Some of the articles exported by India are also produced in and exported from silver-using countries, and other important articles of Indian trade are, it is said, capable of being produced there—notably in China. If there came to be a great divergence between the value of silver and of the rupee, a considerably lower gold price would in China represent the same amount of silver as before, whilst to India it would give fewer rupees. The Chinese would be content to take the same amount of silver—that is to say, the same silver price—that they have hitherto done, so that the Indian producer must rest satisfied with a lower rupee price, or perhaps be driven out of the market altogether through the stress of this competition. One reply given

to this objection is that it involves the proposition that the continuous depreciation of the currency of a country in relation to that of others is advantageous to the commerce of the country whose currency is thus depreciated, and adds to its prosperity. This answer is not absolutely conclusive, because, even if it be true that the cost of production in wages and otherwise would ultimately adjust itself to the fall in the value of silver, yet it is impossible to deny that, until this adjustment has been brought about, the exporter in the silver-using country, who continues to pay the same nominal wages, and whose nominal expenditure for production otherwise remains the same, has an advantage in competition with the exporter who receives a lower price than before, and who can only retain to himself the same advantages by a reduction of nominal wages; and it must be remembered that in a country whose civilisation is backward, and whose industrial institutions are but little developed, the interval may be considerable before such an adjustment can be effected. But, allowing that the argument of those who raise the objection with which we have been dealing is not without foundation, consideration of the experience derived from a study of the history of Indian exports during the period characterised by a fall in the gold value of silver, as noticed in paragraph 27, leads us to doubt whether the suggested advantage is not much less than those who urge the argument suppose.

119. Tea plantations.—Those who are interested in the tea plantations of India, the produce of which is now exported in large quantities, maintain that their industry might be greatly crippled, if not extinguished, by the competition of China and Ceylon if a gold standard were adopted in India only, and silver continued to fall heavily. It is to be observed, however, that the transfer of the commerce in tea from China to India, which has been going on for some years, has taken place, whilst the two countries have shared alike the changes produced by the fall in the value of silver. But it is stated on behalf of the tea planters that, even though their success may be due to the Indian tea better suiting the wants of the consumers, yet the difference in the relative price in gold-using countries of Chinese and Indian tea might be such as to overbalance any advantages possessed by the Indian products, and cause the competition to be a disastrous one for the Indian producer. It must be added that the qualities of the Ceylon tea are much the same as those of Indian tea. It cannot be denied that, if the proposed currency change were adopted in India alone, its tendency might be for a time to benefit the producer in Ceylon, and perhaps the Chinese in his competition with the Indian. To what extent this tendency would prejudice the Indian producer it is impossible to forecast, and, even so far as it did so, it must be remembered that it would not necessarily entail disadvantage on the country as a whole; and having regard to the history of the Indian tea trade, and to its great progress in recent years under existing conditions, we cannot think it likely that any very serious prejudice would result.

120. China might produce what she now imports from India.—We have already referred to the argument that China might in the altered circumstances anticipated produce for her own consumption commodities which she now imports from India. It is alleged that not only would she do this, but that she would also increase her production of cotton and other articles, for which her soil and climate are said to be suitable, and send them into the market to compete with Indian products. To this it is replied, and we think with force, that the want of railways and other means of communication in China, the heavy and arbitrary imports to which production is there subjected, and other causes, deprive these apprehensions of any very serious foundation.

121. Balance of trade and Council bills.—It is further objected that the balance of trade would be disturbed; that the export trade of India would be injured by a gold standard, and that India would thus, *pro tanto*, lose her power of paying her debts; that the Indian Government would in consequence be unable to sell their bills in London; and that they would be obliged to send silver from India at a ruinous loss to pay their gold debt.

122. Export trade.—Council bills.—This objection seems to depend on the question whether the export trade of India will be injured by the proposals of the Government of India, with which we have already dealt in paragraphs 27 and 114 to 120. As to the Council bills, it may be observed that they are only a financial mode adopted as the simplest and best by the Government of India for the purpose of paying a gold debt to England, which in any case they must pay, and which other nations owing gold debts to England pay in other modes. They are orders for the payment of rupees in India, and the same end would be attained if the Government of India bought sterling bills of the exporting merchants in India, and sent them to be cashed on its account in London. Where a country has debts to pay, it must pay them, and it will do so by means of exports, the transaction being effected in whatever methods are found to be most convenient.

123. India must pay her debts in whatever is the most convenient form.—So far as concerns their effect on the import of silver into India, the Council bills now compete with silver; the closing of the mints to silver would relieve the Council bills from this competition, and the immediate effect would be a tendency for the bills to sell at a higher price. The merchant wishing to pay for Indian goods would have to pay more gold for the Council bills. If their price should rise so far as to make the business of buying Indian goods unprofitable, it would no doubt, *pro tanto*, check the export trade of India, and the price of the bills must fall. But it would only fall so far as would be necessary in order to make the trade again profitable. In short, India must pay her debts by exports, and the Indian Government cannot in any way avoid whatever expense is necessary in order to pay them. That these exports should ever consist of silver, depreciated as silver is in the Western world, is highly improbable; but, if this

should turn out to be the case, it would be because silver was the article which India could best spare.

124. Currencies of Native States.—Fear has been expressed that the restriction of the coinage of rupees at the British mints would lead to an increase of the use of the coins of Native States in the British provinces. There are numerous Native States in different parts of India which exercise the right of coining, a privilege of which they are most tenacious, regarding it as an indication of sovereign authority. The currencies are very various in their details, the chief silver coin being the rupee, but with many variations in intrinsic value in the different States. In 1835, when the existing system of currency was adopted, a list of the various rupees then existing included no less than 300 different coinages (many, no doubt, obsolete), for the most part showing greater or less variations of value *inter se.*

125. The attempt made to facilitate the adoption of a common currency throughout India by an Act passed in 1876 has had no material effect. It provided that on a Native State agreeing to abstain from coining for at least thirty years, and not to allow coins resembling those of British India to be struck under its authority, the Government of India would coin for the State rupees identical in weight and fineness with those of British India, but with a device differing from that before used by the State. Such coins would be legal tender in British India. Up to the present time only four of the minor States have availed themselves of the provisions of this Act.

126. Sufficient information on the subject of the currencies of the various States is not available to admit of our giving any precise account of them, but there is reason to think that their issues are not on a scale of any considerable magnitude. The coinage of Hyderabad, the largest of the Native States, is stated to have been in 1887-88 816 tolas of gold and 15,051 tolas of silver, and in 1888-89 784 tolas of gold and 17,76,421 tolas of silver, the tola representing the weight of a rupee; the value of the Hyderabad rupee, commonly called the Halli Sicca rupee, is about 14 per cent. less than that of the rupee of British India. The Baroda State coined 8 lakhs of rupees in 1883-84 and 9 lakhs in 1884-85, but in the three following years there was no coinage; new machinery for the mint was supplied in 1891. The Kashmir mint appears to be no longer in operation, and the States of Mysore and Rewah also are said to have no mints. The coinages of Holkar's Government at Indore, of Bhopal, and of Travancore are reported to be very small in amount.

127. On the whole, it appears that the annual addition to the coinage of the Native States is of little importance. The coins of these States have a free circulation among the population of the border districts of those States and the British provinces, and at times are found at considerable distances from their place of origin. They are, however, always liable to a charge for discount when circulating beyond the State from which they issue, and in no case

are received at British treasuries, by the railways, municipalities, or other local bodies, nor are they legal tender in British territory.

128. On this subject the Government of India, in a telegram of the 16th of March 1893, stated their opinion that they could easily overcome any difficulty that might arise in connection with rupees coined under the Native Coinage Act, 1876, before mentioned, and that they did not think that any serious difficulties could arise in connection with the coinages of Native States generally.

129. Ceylon and Mauritius.—We have had evidence from persons interested in the trade of Ceylon expressing apprehensions that if the proposed change of standard were to be made in India, and the present currency arrangements were to be continued in Ceylon, the effect would be prejudicial to the trade of that island. These apprehensions are of the same nature as those we have already examined on the part of the planters in India. It is obvious that independently of these apprehensions, both Ceylon and Mauritius, which have the rupee as their standard coin, which have no mints of their own, and which import their rupees from India, would be affected by the closing of the mints and by the adoption of a gold standard in India. It would in that event be open to the Governments of those Colonies to acquiesce in the action of India, or to establish currencies of their own, with or without local mints. If they should adopt a currency of their own, and if in India the rupee should in consequence of the proposed changes rise above its silver value, it would become profitable to export Indian rupees from those Colonies to India. Such an export would operate in the same way as a release of the hoards of coined rupees in India, and might, so far as it goes, delay the rise in the value of the rupee. But, according to the best information we can obtain, the stock is not so large as to be likely to have any considerable disturbing influence. It is no part of our duty to advise what action should be taken by the Colonial Governments, except to point out that they ought not to allow any coins which they issue to be so similar to the Indian rupee as to be mistaken for it, and thus to become current in India.

Objections (b) supposing the ratio to be raised materially above the present level.

130. Objections on the assumption that the ratio is raised materially above the present level.—We have been hitherto dealing with the proposals of the Indian Government on the assumption that exchange is at once fixed at a point not materially above its present level. The suggestion of the Government of India is that no ratio should be fixed immediately on the closing of the mints. Their proposal to take power to declare that English gold coinage shall be legal tender in India at a rate of *not less than* 13⅓ rupees to the sovereign would, if acted upon, prevent the exchange from rising to any great extent above 1*s*. 6*d*.—that is, a ratio of silver to gold a little less than 20 to 1. As the

present exchange value of the rupee is 1*s.* $2\frac{3}{4}d.$, and the ratio of silver to gold about 24 to 1, the Indian Government, though it may be that they would act gradually and tentatively, suggest the possibility of raising the ratio materially above the present level.

131. We have now, therefore, to consider what are the objections to these proposals on the assumption that the exchange were so raised.

132. The same objections as if the ratio were not raised.—All the objections which have been urged as existing in the case of the assumption that the ratio were fixed at a point not materially above the present level are at least equally applicable in the case of that which we have now to consider; but the answers which have been given to them in the former case are not all of equal force where the ratio has been materially raised.

133. Spurious coinage, trade, inconvertible currency.—The dangers of spurious coinage and of depreciation of Indian hoards must increase in proportion to the difference between the value of the rupee and the market value of silver; and the trade difficulties due to a rising exchange, such as they are, would, of course, be the greater the higher the ratio was taken. Moreover, the difficulty of maintaining an inconvertible token coinage as full legal tender at a par value tends to increase with the difference between the legal value of the token coin and the metal it contains; but the cases of foreign currencies quoted above show that difficulties similar to those which are apprehended in the case of India have been successfully encountered.

134. Objections founded on effect upon rupee prices and fixed burdens.—We pass to the objections founded upon the effects on rupee prices, on taxation, and on other fixed burdens. These effects would be such as result from an appreciating currency, namely, first, to make prices lower than they would otherwise have been; then, though more slowly, to lower money wages, and to increase the burden of debts and of all fixed payments. It has been urged in answer to this that, whatever these evils may be, they are not greater than those which have in recent years been experienced from a depreciating currency, namely, prices higher than they would have been but for such depreciation, and debts and other just burdens lightened, to the benefit of the persons who pay, and to the injury of those who receive, including the Government. It has also been urged that if future appreciation were due to the act of the Government, past depreciation has also been due to the adoption by the Government of an unstable and depreciating standard. But, even assuming that these answers are true in point of fact, it is no less true that, since the adoption of the silver standard in 1835, the depreciation of the silver currency has arisen from causes over which the Government have exercised no control, whereas any appreciation resulting from the raising of the rupee would be due to the direct action of the Government.

135. It is impossible in view of these considerations not to come to the conclusion that to close the mints for the purpose of raising the value of the rupee is open to much more serious objection than to do so for the purpose of preventing a further fall.

136. Injury to Eastern trade.—It has been represented to us by the China Association, the Chambers of Commerce at Hong-Kong and Singapore, and others interested in the Eastern trade that a change, such as has been proposed by the Government of India, would be likely to be prejudicial to their interests. Although some of the facts to which we have already drawn attention indicate that the apprehensions expressed are excessive, and although some of the arguments which we have adopted are not inapplicable to their case, we have not thought it within the limits of Your Lordship's reference to enter in detail upon the considerations suggested by these representations.

Alternative Schemes.

137. Charge on silver.—Amongst the suggestions made for preventing a further fall in the value of the rupee, for counteracting the effect of the fall which has already taken place, and for adding to the resources of the Government of India is a proposal to impose a charge on silver, which might take the form either of an increased seignorage on the coinage of the rupee or of a duty on all silver imported. It is claimed for this proposal that it would avoid direct and obvious interference with the standard of value, whilst it would bring in additional revenue to the Government. It is therefore desirable to examine it carefully.

138. Seignorage. Fixed in amount.—Let us first assume the charge to be a seignorage. In that case, it would be imposed only on the silver brought to be coined. It might take either of two forms, *viz.*, a fixed charge of so much per ounce, or a charge varying inversely as the gold value of silver, so as to keep the rupee at a certain fixed ratio to gold. A fixed seignorage would be no remedy for a fluctuating exchange, because, whatever might be its present effect, it would fail to maintain a parity of exchange between the rupee and the sovereign if silver should fall further or should rise in value; and, although it might afford some present relief, a continued fall in exchange would leave India subject to the same difficulties as before.

139. Varying inversely as the gold price of silver.—A seignorage varying inversely with the gold value of silver is not open to the same objection. If this were adopted so as to make the gold price of a given weight of silver *plus* the duty always equal to a given weight of gold, it would, no doubt, tend to maintain the rupee at a fixed ratio to the sovereign. But to provide from time to time for the necessary alterations in such a varying seignorage, so as not to embarrass trade or to encourage undesirable speculation, would be an administrative function of some difficulty. An intermediate course might be taken, making

the seignorage vary, not with the daily rate of exchange, but at fixed intervals, say, from year to year, so that the annual charge should vary inversely as the annual average gold value of silver for the preceding year. Though, judging by recent experience, this method would lessen considerably without, however, entirely removing the administrative difficulties above mentioned, yet towards the end of the term for which the seignorage had been fixed speculators would be encouraged either to pour silver into India or to abstain from importing it, according as they expected the seignorage to be raised or lowered.

140. Indirect method of altering the Standard.—The imposition of a seignorage necessarily enhances in an artificial manner the value of the rupee above the intrinsic value of the silver it contains, and tends to reduce the amount coined. Many of the objections, therefore, which have been urged to the proposals of the Government of India apply equally in principle to such a scheme. It is, in fact, an indirect method of attaining the end which the Indian Government propose to attain by closing the mints.

141. Regarded as a mode of raising revenue.—Unsatisfactory.—A 10 per cent. seignorage—that is, an addition of 8 per cent. to the present rate,—even on the assumption that its imposition had no effect in reducing the amount coined, would only on the average coinage since 1875 produce annually about Rx. 600,000; and therefore, regarded as a mode of raising revenue, the relief afforded to the Indian Exchequer would not be sufficient to meet the difficulties which the Government have to encounter. It is impossible to anticipate that with so heavy a seignorage the amount coined would be as large as on the average of recent years; nor could any fixed amount be relied on, since it would depend on the state of the exchange, and on the quantity of silver brought to the mint. It is, in fact, open to the objection in principle which applies to many other forms of taxation imposed for purposes other than that of revenue, *viz.*, that in proportion as it effects the object of restricting the coinage of silver, it ceases to be profitable as a source of revenue.

142. Duty on silver imported.—It remains for us to consider the effect of imposing a duty on all silver imported, whether for coinage or otherwise. Such a duty would tend to restrict the supply of uncoined as well as coined silver; but, looking to the fact that nearly all the silver imported in recent years has been coined, this difference is not at the present moment of great importance. Subject to this distinction, the observations we have made on the proposals for a seignorage apply also to the proposal to levy a duty on uncoined silver, with the addition that such a tax would be difficult to enforce, and would be an encouragement to smuggling; and that, if it were made to vary constantly with the gold price of silver, the administrative difficulties would be even greater.

143. Coinage of heavier rupees.—The coinage of a new rupee of greater weight than that at present existing has been suggested as a remedy for the difficulty. If for this purpose the plan

were adopted of recoining the existing rupees, it is evident that the expense, which must be calculated on at least 1,000 to 1,500 millions of rupees, would be very heavy, even if the measure did not attract to the mints hoards in excess of the amount in circulation; and, after the recoinage had been completed, there would be no security that it would be effectual, since a further fall in the gold value of the rupee would produce difficulties of the same kind as have now arisen. If, on the other hand, in addition to the existing rupees, heavier rupees were issued, there is the objection that, for some time at any rate, two kinds of coin would be in circulation, of different intrinsic worth, yet professedly of the same value; and there does not appear to be any advantage in this plan over that proposed by the Government of India.

144. Various schemes.—Other plans which have been suggested are the introduction of a gold standard with a gold currency, the ratio of the gold and silver coins being notified from time to time according to the market rates of exchange; the adoption of a gold standard with a very high unit, rupees being made token coins, and currency notes of large denomination being issued for gold alone, but payable in either gold or rupees; the issue of currency notes expressed in gold, but exchangeable only into rupees at the foreign exchange rate of the day; the establishment of a gold standard without a gold coinage based on the credit of a reserve to be held by the Bank of England in India; the gradual introduction of a gold standard by placing the rupee debt on a gold basis, and providing for the discharge of debts partly in gold and partly in silver, the proportion of the former being annually increased until the whole became fixed in gold; the adoption of a given amount of gold bullion as a standard for foreign and wholesale transactions, leaving the coins to be used as tokens for internal trade; the declaration that rupees shall be a legal tender in the United Kingdom; the issue of coins of mixed gold and silver; the basing of the currency system on a certain amount of Government sterling stock; the adoption of independent standards of gold and silver to be in use at the same time.

145. We deem it unnecessary to do more than indicate in the briefest manner the nature of these proposals. Some of them are not within the power of the Government of India, and others are impracticable for various reasons; while no one of them appears to be so free from objection as to justify us in advising Your Lordship to reject in its favour the proposal of the Government of India.

Possible modifications of the proposals of the Government of India.

146. Possible modifications of proposals.—Your Lordship will observe that we have given most careful and anxious consideration to the objections which have been urged against the scheme of the Government of India; we feel that some of them have weight, and we regret that, in the opinion of that Government, it should be necessary to propose a measure which would undoubtedly

be attended with some risks and inconveniences. We proceed to consider whether, in case it were decided to adopt such a proposal as that made by the Government of India, it would be possible by any modifications to remove or diminish the objections to which we have referred.

147. Provision against a sudden great rise in exchange.—It appears to be desirable that any such scheme should afford security against any sudden and considerable rise of exchange. If the closing of the mints were thought likely to lead to such a rise, the opposition to the measure would, no doubt, be greatly augmented. In all probability the cessation of free coinage of silver would be immediately followed by a fall in the price of that metal. If at the same time exchange rose considerably, the divergence between the rupee and its intrinsic value would become at once very marked. The difficulty of maintaining the rupee at its higher exchange value might be increased, and the apprehensions of disaster which are entertained, even if they be exaggerated or unreal, would be intensified.

148. Moreover, the rise in exchange would be calculated to lead to a fall in the price of Indian produce. And, if this were seen to follow, and believed to be caused by the action of the Government, public opinion might be disturbed and the situation might become critical. The view has been expressed that, even though the native producers might not be likely to be actively hostile to a scheme which left prices unaffected, they would be far from indifferent, and the state of things might become dangerous if prices began to fall very sensibly.

149. What, then, would be the effect of the scheme suggested by the Government of India? Closing the mints, even if the Government of India were to issue the proposed notification that gold coins would be made legal tender at a rate of $13\frac{1}{3}$ rupees to the sovereign, might bring about a rise in exchange to the level thus indicated, *viz.*, 1*s.* 6*d.*, per rupee. It is true that those who think that exchange would not for a considerable time rise at all, and that even the existing ratio might not be maintained, may be right in their anticipations. But it must be admitted that on such a point no one can predict with certainty; exchange might rise suddenly and considerably, unless the Government were to interfere actively to prevent it; and the public would not feel any certainty as to the course they would take.

150. Ratio for coinage of rupees on tender of gold at the mints.—The scheme might, however, be so modified that the exchange could not immediately rise much above its present level. It might be provided that the mints should be closed to the public for the coinage of silver, but should be used by the Government for the coinage of rupees if required by the public in exchange for gold, at a ratio to be fixed in the first instance not much above that now prevailing, say 1*s.* 4*d.* the rupee. Any fear of a considerable rise would thus be allayed, and any evil effects of such a

rise would be prevented. Moreover, even if silver fell, the divergence between the nominal and the intrinsic value of the rupee would not be so great as if exchange at the same time rose. There would be these additional advantages: First, the currency would not cease to be automatic. Next, it would be a less violent step than closing the mints altogether. They would practically remain open, subject to certain conditions. It would be the smallest departure from the *status quo* which could accomplish the object the Government of India have in view. Besides these advantages, there would be the further gain, that it would still leave the volume of the rupee coinage dependent on the wants of the people of India; and the fact that rupees might continue to be cioned would tend to prevent silver falling as much as would be the case if it were supposed that the coinage of rupees was to cease altogether.

151. The Government of India have expressed the opinion that there would be no practical difficulty in carrying such a modified scheme as this into effect. It would not, of course, be essential to the plan that the ratio should never be fixed above 1*s.* 4*d.*; circumstances might arise rendering it proper, and even necessary, to raise the ratio; and the Indian Government might be empowered to alter it with the sanction of the Secretary of State. Such a scheme would, indeed, in the first instance, be tentative, and would not impede further action if circumstances should render it desirable.

152. Acceptance of gold coins in payment of public dues.—It would be consistent with the scheme, and would serve as a means of familiarizing the public with the use of a gold currency, if the Government were to accept gold coins at the same ratio in payment of all dues.

153. Inasmuch as the course to be pursued in relation to the matter referred to us will come before Her Majesty's Government for decision, the Chairman thinks it right to abstain from taking any part in determining what recommendations should be made to Your Lordship.

154. We desire to express our high appreciation of the benefit conferred upon us by the appointment of Mr. Waterfield to act as Secretary to the Committee. His knowledge, ability, and zeal have been of the greatest assistance to us throughout our protracted deliberations.

HERSCHELL.

LEONARD COURTNEY.

T. H. FARRER.

REGINALD E. WELBY.

ARTHUR GODLEY.

R. STRACHEY.

B. W. CURRIE.

Recommendations of the Committee.

155. Recommendations of the Committee.—It remains for us to state the conclusions at which we have arrived. While conscious of the gravity of the suggestion, we cannot, in view of the serious evils with which the Government of India may at any time be confronted if matters are left as they are, advise Your Lordship to overrule the proposals for the closing of the mints and the adoption of a gold standard, which that Government, with their responsibility and deep interest in the success of the measures suggested, have submitted to you.

156. But we consider that the following modifications of these proposals are advisable. The closing of the mints against the free coinage of silver should be accompanied by an announcement that, though closed to the public, they will be used by Government for the coinage of rupees in exchange for gold at a ratio to be then fixed, say 1*s.* 4*d.* per rupee; and that at the Government treasuries gold will be received in satisfaction of public dues at the same ratio.

157. We do not feel ourselves able to indicate any special time or contingency when action should be taken. It has been seen that the difficulties to be dealt with have become continually greater; that a deficit has been already created, and an increase of that deficit is threatened; that there are at the present moment peculiar grounds for apprehension; and that the apprehended dangers may become real with little notice. It may also happen that if action is delayed until these are realized, and if no step is taken by the Indian Government to anticipate them, the difficulty of acting with effect will be made greater by the delay. It is obvious that nothing should be done prematurely or without full deliberation; but, having in view these considerations, we think that it should be in the discretion of the Government of India, with the approval of the Secretary of State in Council, to take the requisite steps if and when it appears to them and to him necessary to do so.

LEONARD COURTNEY.
T. H. FARRER.
REGINALD E. WELBY.
ARTHUR GODLEY.
R. STRACHEY.
B. W. CURRIE.

HENRY WATERFIELD,
Secretary.

It seems to me that our judgment of what the Home Government should do in reference to the proposals of the Government of India must depend upon the view we take of the cause of the diver-

gence in value that has arisen between gold and silver. The Indian Government has to make large annual payments in gold, whilst its receipts are in silver. Has gold become more valuable in itself or silver less valuable in itself, or if both movements have happened, which has been relatively greater? If gold has become more valuable, the burdens of India have become greater than was contemplated or intended, and we must ask ourselves whether they can be in any degree reduced. If silver has become less valuable, the taxation of India is made lighter, and we may freely examine the means, direct or indirect, of raising it. If an intermediate hypothesis is adopted, our way of viewing the problem must be modified accordingly. In our Report we have not examined this preliminary question, but I hold it the first to be determined. For reasons upon which I do not now enter, I have come to the conclusion that the divergence between gold and silver has been to a large extent due to an appreciation of gold; and this opinion necessarily affects my judgment of the policy of the Indian Government, which is to adopt a gold standard instead of one of silver. This is to accept as unalterable, if not to intensify, the aggravated burden thrown upon India. It may be that no other course is possible, but the Home Government should ask itself whether it is through its own action that no other course is possible, and whether the Indian Government might not propose a very different course if there was any chance of its being favourably considered by the Supreme Government. I am myself drawn to the conclusion that the Home Government is the greatest obstacle, perhaps the only substantial obstacle, to the establishment of an international agreement for the use of silver as money, which, without attempting to restore the position of twenty years since, would relieve India from the anxiety of a further depreciation of its revenue in relation to its liabilities. The problem may be thus stated:—The Indian Government asks permission to adopt a certain course, but, as is well understood, not the course it would of its own free will first desire to be adopted. In considering whether the course actually proposed should be sanctioned, we cannot refuse to consider whether there are invincible obstacles to the entertainment of the course which would be the first preference of India.

If I am to put aside the previous question, and confine myself to the proposition whether the Indian Government should be allowed to suspend the free coinage of silver, so as to enhance the value of the coined rupee till it reached a certain relation to the sovereign, such as 1 to 15 (1*s.* 4*d.*) or 1 to $13\frac{1}{3}$ (1*s.* 6*d.*), I concur in the report of my colleagues, subject to the following reservation:—In paragraph 139 I think we have overrated the difficulty and delicacy of the administrative function involved in the plan there discussed. I believe action would be fairly simple if the plan were practically tackled. The mints of India are not so numerous as to prevent a daily telegraphic message of the seignorage to be charged, if such frequency should be deemed necessary. The embarrassment to which a person in London wishing to make a remittance in India

would be exposed from his uncertainty as to what the seignorage would be when silver reached an Indian mint would be of the same character as his present embarrassment in not knowing what the exchange would be when silver reached India if he sent it out.

LEONARD COURTNEY.

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1. In the year 1878 the Government of India made a proposal that the mints should be closed against the free coinage of silver until the rupee should rise in value to 2*s.*, or one-tenth of an English sovereign. In making this proposal, and on other occasions, the Indian Government expressed themselves in very strong terms* concerning the dangers and difficulties, present and prospective, caused to India by the fall in silver. A Committee appointed by the Secretary of State, of which we were members, reported unanimously against the above-mentioned proposals, and it was rejected by the Home Government.† Further experience shows that, whilst the views expressed by the Government of India concerning the future of silver have been fully justified by the fall which has since taken place, the present condition of India is scarcely such as to justify their estimate of the difficulties and dangers to the country which they believed would arise from it.

2. The following facts relating to the recent progress of India are taken from a paper read by Sir W. Hunter (one of the greatest existing authorities on the subject) at the Society of Arts on the 16th February 1892:

"Between 1881 and 1891 the whole number of the army had been raised from 170,000 to 220,000, and the number of British soldiers in it from 60,000 to 71,000, or, including reserves, volunteers, etc., to very much more. Many large and costly defensive works had been constructed both on the North-West frontier and on the coasts. In recent years almost all public buildings have been reconstructed on a large scale.

"Railways, both military and commercial, have been very greatly extended. Notwithstanding these extraordinary expenses, there were during the 25 years which followed 1862, 14 years of surplus and 11 years of deficit, yielding a net surplus of Rx. 4,000,000. In 1889 the public debt of India, exclusive of capital invested in railways, showed a reduction since the mutiny period of Rx. 26,000,000. The rate at which India can borrow has been reduced from 4 or 5 per cent. to a little over 3 per cent. The revenue of India, exclusive of railways and municipal funds, has grown between 1856-57 and 1886-87 from Rx. 33,378,000 to Rx. 62,859,000, and in 1891 it had increased to Rx. 64,000,000, or, including railways and irrigation receipts, to Rx. 85,750,000, and

*See despatch of 9th November 1878, para. 22, and despatch of 4th September 1886, para. 24.

† See Treasury letter of 24th November 1879.

this increase is due to the growth of old revenue rather than to new taxation. Further, whilst the rent or land tax paid by the people has increased by one-third, the produce of their fields has more than doubled in consequence partly of higher prices, and partly of increase in cultivation. Further, in 1891 there were nearly 18,000 miles of railway open, carrying 121,000,000 of passengers and 26,000,000 tons of goods, and adding a benefit to the people of India, calculated as far back as 1886, at Rx. 60,000,000. Further, the Indian exports and imports at sea, which in 1858 were about Rx. 40,000,000, amounted in 1891 to about Rx. 200,000,000, and the produce thus exported has increased in quality and variety no less than in amount."

3. Considering facts such as these, we should even now have difficulty in recommending the closing of the Indian mints against the free coinage of silver if it were not for the circumstance that a further heavy fall in silver is possible, and in certain contingencies imminent, and that any such fall may bring with it mischiefs and difficulties much greater than any which have yet been experienced.

4. Under these circumstances, having regard to the part we have already taken in this matter, as well as to the present exigencies of the case, we are anxious to state more fully and explicitly than is done in the report we have signed what is the full effect of the immediate step which we have agreed in recommending, and what precautions are in our opinion desirable with a view to its ulterior consequences.

The step recommended is that the Indian Government should be empowered to close the Indian mints against the free coinage of silver until the rupee rises in value, so as to stand at a given ratio with the sovereign; such ratio to be little above the ratio which has been current, say 1*s*. 4*d*., and that they should then be required to give rupees at that ratio for all gold brought to their mints. The immediate effect of this step will be to alter the Indian measure of value. As long as the Indian mint is open, the measure of value is the market value of the weight of silver contained in the rupee; but, as soon as the mint is closed, we can no longer be sure that this will be the case. Further, so soon as the rupee has risen to the given ratio, the fraction of an English gold sovereign represented by 1*s*. 4*d*. will become the measure of value. This is in itself a most important change.

5. To alter the measure of value by substituting one metal for another is at all times a matter of great gravity, and to do so at a time when the relations between the two metals are in a state of constant fluctuation renders the alteration still more serious.

6. It is, however, to be observed that the step which we recommend will produce the least possible immediate change. Its object is not so much to raise the gold value of the rupee as to prevent a further fall. It does not materially alter the present relations between debtor and creditor, but, on the contrary, prevents those relations being altered in the future by a further fall. Moreover,

it provides a means whereby, in case there should be a demand for currency, that demand will be supplied automatically, and not at the discretion of the Indian Government.

7. This closing of the mints, however, is only the first step in the process contemplated by the Indian Government, and that process will not be complete until gold is made full legal tender, and is received into the Indian currency as freely as gold is received in England, or as silver is now received in India. This may be effected either by the free coinage of gold at the Indian mints or by the free reception under arrangement with the Imperial Government of gold sovereigns coined in England or in Australia as legal tender currency of India. When this is done, the change will be complete, and India will then have a gold standard of value, and a gold automatic currency, the quantity of which will depend on the demand for it. What that demand may be is uncertain. Sir D. Barbour estimates the outside of the quantity needed to maintain the gold standard at 15,000,000*l.*, or one-fifth in value of the estimated present rupee currency. But, whatever the precise amount, the gold currency is not expected to be more than a small fraction of the actual currency in circulation.

8. This currency will consist of rupees, each of which is intended to circulate, not at the value of the silver contained in it, but at the value of the gold contained in the fraction of the sovereign (*1s. 4d.*) which it represents. With the exception of the small quantity of gold in actual circulation, the currency of India will thus become a token currency of unparalleled magnitude; and if the market value of silver should fall considerably, its value would become very much greater than the value of the silver contained in it. Under such circumstances, it will to a great extent resemble a paper currency, and, if it were not made exchangeable for gold on demand, would resemble in many respects an inconvertible paper currency. The question then arises whether it is certain that such a currency will be maintained at its gold value without further precautions.

9. It is no doubt true that, until the rupee has risen in value to this adopted ratio, the scheme will not have come into full operation, and that, when it has come into full operation, the restriction placed upon the issue of silver rupees will tend to keep the rupee currency at the fixed gold value. But it may well be questioned whether this restriction is in itself a sufficient guarantee that this gigantic token currency will, under all circumstances, be kept at par value. Sir David Barbour himself holds that eventually, if the scheme is to be successful, gold when required must be given for the rupee either without a premium or at a small premium.

10. It is, of course, obvious that a great country like India, if she undertakes a token currency, must maintain its value and discharge her obligation by making it reasonably certain that, where gold is needed in exchange for rupees, it will be possible to obtain it at the fixed ratio.

11. It has been argued that this object might possibly be effected without requiring the Government of India to give gold for silver at that ratio, and without the public confidence in their ability to do this which would arise from their accumulating and possessing a stock of gold available for the purpose. Instances may, no doubt, be selected in which Governments have maintained their inconvertible token currency at, or nearly at, par without these precautions. But a silver token currency, though not in form a promise to pay, really implies an obligation to maintain its par value: and prudence as well as experience suggest that this obligation should be supported by the obvious means of fulfilling it.

12. The obligation on the Government to coin silver rupees when the rupee is at 1*s*. 4*d*. does not in itself carry with it a corresponding obligation on the Government to give gold for rupees. It may not therefore be necessary to provide a reserve of gold before that exchange is reached. If it is not reached under the measure proposed, no gold reserve will be needed; but if the measure is operative, gold will probably flow in, and will replace silver as the reserve against the Government paper issue. If gold thus flows in automatically, the Indian Government will be thereby enabled to accumulate a moderate reserve; but, even if it does not, a reserve should, we contend, be provided before the Indian Government takes the final step of announcing gold as the standard, coupled with the correlative obligation to give gold for silver.

13. What amount of gold reserve may be necessary it is difficult to say, but in order to have desired effect, it must be substantial. Nor, considering that it will in all probability be generally resorted to for purposes of export, is it necessary to decide in what form or in what place it should be kept. The circumstances of India are favourable for the accumulation of the necessary stock. India imports more of the precious metals than she exports: her inhabitants no doubt possess already a stock of uncoined gold: and, if the Indian Government receive gold in payment of debts due to them, gold ought to come to their treasuries.

14. At any rate, the expense necessary to procure and retain the requisite amount is one that cannot be avoided by any Government which desires to maintain the credit of its currency, and will be insignificant compared to the loss of which the Indian Government now complain.

15. Under these circumstances, we could not join in the recommendation contained in the report without at the same time recommending that the Government of India should, in view of the ultimate adoption of the whole of their plan, be prepared to secure the convertibility of their token silver currency, and should with that object accumulate a sufficient reserve of gold.

16. We think it right to add that the questions whether gold has become more valuable in itself or silver less valuable in itself, or whether both movements have taken place, and to what extent each movement has gone as well as the further question between bimetallism on the one hand and a universal gold standard on the

other, are questions of which we have taken no notice, as we do not think that they fall within the scope of the reference to us.

T. H. Farrer.

R. E. Welby.

While cordially concurring with the views of my colleagues so far as they support the proposals of the Government of India, I should have preferred to approve those proposals without imposing the conditions that the closing of the mints should be accompanied by an announcement that rupees will be coined in exchange for gold at the ratio of 1*s*. 4*d*.

It will be admitted that in a matter of this kind the minimum of State interference is desirable.

The only excuse for any action on the part of Government is that the evils from which they are suffering are becoming intolerable, and that, apart from the closing of the mints, no practical remedy has been proposed or is attainable.

In my opinion the proper course for Government to adopt is to issue a proclamation to the effect that,—

Having regard (1) to the redundancy of silver money in India as evidenced by the accumulation of rupees and paper currency in the banks, and (2) considering the uncertain policy of other nations with respect to silver, the Governor General in Council has resolved to suspend for the present the coinage of silver.

One effect of such a measure must necessarily be that the London exchange banks in tendering for Council bills will be compelled to quote the price in sterling which they are willing to pay. Another probable effect will be that gold will be sent to India in increased quantity on private account in order to be exchanged into rupees; and it appears to me that the price in each of these cases, when extended over a considerable period of time, and after a certain degree of stability has been attained, will afford the best guide to Government in estimating the gold value of the rupee, whenever they are called upon to open their mints to the coinage of gold.

The Government of Austria-Hungary closed their mints to the free coinage of silver in 1879, but did not declare a ratio between gold and silver till 1892. It seems likely that an interval of time more or less prolonged may elapse before the Government of India will be in a position to declare a ratio, having regard to the great uncertainty of the effect which its action may produce upon the rate of exchange.

I prefer to leave full discretion to that Government to take such measures as occasion may require and experience may dictate, subject to the consent of the Secretary of State in Council.

I fear that any arbitrary action on the part of Government in a matter respecting which it is impossible that all the facts can be

present to their consideration might lead to reclamations both from the public creditor and from others whose interests depend upon Indian exchange, and I am unwilling to take the responsibility of attempting to fix a rate if the object can be practically accomplished by the natural action of the market.

Moreover, I fail to see what advantage would be gained by selecting the ratio of 22·37 to 1 (one and fourpence the rupee) rather than that of 18·22 to 1, which has been adopted with apparent success in Austria, or that which is in use among other nations.

If contrary to expectation exchange should rise suddenly in an inconvenient degree, I would meet the difficulty in the way proposed by the Government of India (quoted at paragraph 47 of the Committee's Report) by declaring that English gold coins shall be legal tender in India at a rate to be fixed by them.

B. W. Currie.

Report of the Indian Currency Committee, 1898.

INDIA OFFICE,
7th July 1899.

To

THE RIGHT HONOURABLE LORD GEORGE HAMILTON, M.P.,
SECRETARY OF STATE FOR INDIA.

1. In your letter of the 29th April 1898, your Lordship referred to us for consideration the proposals of the Government of India* for making effective the policy adopted by Her Majesty's Government in 1893 and initiated in June of that year by the closing of the Indian Mints to what is known as the free coinage of silver. That policy had for its declared object the establishment of a gold standard in India; and in inviting us to consider whether this object could best be attained by the specific measures proposed by the Government of India or otherwise, your Lordship indicated the scope of our inquiry in the following words†:—"It will be the duty of the Committee to deliberate and report to me upon these proposals and upon any other matter which they may regard as relevant thereto, including the monetary system now in force in India, and the probable effect of any proposed changes upon the internal trade and taxation of that country; and to submit any modifications of the proposals of the Indian Government, or any suggestions of their own, which they may think advisable for the establishment of a satisfactory system of currency in India, and for securing, as far as is practicable, a stable exchange between that country and the United Kingdom."

2. For the purposes of our inquiry we have held 43 meetings and examined 49 witnesses. The notes of evidence, together with statistical tables and other important information bearing on the subject of inquiry, have already been communicated to your Lordship‡; and we now proceed to report the conclusions which we have reached upon the questions referred to us.

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* C.—8840, "Correspondence respecting the proposals on currency made by the Government of India."
† C.—9037, p. iii.
‡ C.—9037; C.—9222; C.—9376.

I.

The Monetary System of India.

3. In order to explain the monetary system now in force in India, it is desirable to record certain salient facts of the history of Indian currency.

4. At the beginning of the present century no uniform measure of value existed in British India. Some parts of India (*e.g.*, Madras) maintained a gold standard and currency; elsewhere, as in Bengal, a silver standard obtained, with gold coins in concurrent circulation; throughout India the coins, whether of gold or silver, differed in denomination and differed in intrinsic value even within the same district. Out of this confusion arose the demand for an uniform coinage, a demand to which the Court of Directors of the East India Company gave their approbation in the important Despatch on Indian currency addressed by them to the Governments of Bengal and Madras on 25th April 1806.* It is important to observe that the Directors, while "fully satisfied of the propriety of the silver rupee being the principal measure of value and the money of account," by no means desired to drive gold out of circulation. "It is not by any means our wish," they said, "to introduce a silver currency to the exclusion of the gold, where the latter is the general measure of value, any more than to force a gold coin where silver is the general measure of value." Nevertheless the first fruits of the policy of 1806 were seen in the substitution in 1818 of the silver rupee for the gold pagoda as the standard coin of the Madras Presidency, where gold coins had hitherto been the principal currency and money of account. In 1835, when the present silver rupee was formally established as the standard coin of the whole of British India, it was enacted that "no gold coin shall henceforward be a legal tender of payment in any of the territories of the East India Company."

5. But, though gold had ceased to be a legal tender in India as between private individuals, the coining of gold mohurs (or "15 rupee pieces") was authorised by the Act of 1835, and a Proclamation of 13th January 1841 authorised officers in charge of public treasuries "freely to receive these coins at the rates, until further orders, respectively denoted by the denomination of the pieces." As the gold mohur and the silver rupee were of identical weight and fineness, this Proclamation represented a ratio of 15 to 1 between gold and silver. In 1852† it was held by the Directors of the East India Company, on representations from the Government of India, that the effect of this Proclamation "has been, and is likely to be still more, embarrassing" to the Government of India. "The extensive discoveries of gold in Australia having had the effect of diminishing its value relatively to silver, holders of gold coin have naturally availed

* H. of C. No. 127 of 1898.
† H. of C. No. 254 of 1860, p. 46.

themselves of the opportunity of obtaining at the Government treasuries a larger price in silver than they could obtain in the market." Consequently, on 25th December 1852 there was issued a Notification* withdrawing the above provision of 1841, and declaring that, on and after 1st January 1853, "no gold coin will be received on account of payments due, or in any way to be made, to the Government in any public treasury within the territories of the East India Company."

6. In 1864,† the Bombay Association (representing the native mercantile community of Bombay) and the Chambers of Commerce of Bengal, Bombay and Madras having memorialised the Government of India for a gold currency, the Government proposed "that sovereigns and half-sovereigns, according to the British and Australian standard, coined at any properly authorised Royal Mint in England, Australia, or India, should be made legal tender throughout the Brtish dominions in India, at the rate of one sovereign for 10 rupees; and that the Government currency notes should be exchangeable either for rupees or for sovereigns at the rate of a sovereign for 10 rupees, but that they should not be exchangeable for bullion." The Imperial Government, while unwilling to make the sovereign a legal tender, saw "no objection to reverting to a state of matters which prevailed in India for many years, namely, that gold coin should be received into the public treasuries at a rate to be fixed by Government and publicly announced by Proclamation." It was considered that this experimental measure "will, as far as it goes, facilitate the use of the sovereign and half-sovereign in all parts of India; it will pave the way for the use of a gold coinage in whatever shape it may ultimately be found advisable to introduce it; and at the same time, it establishes a preference in favour of the sovereign." Accordingly, on 23rd November 1864, a Notification was issued that sovereigns and half-sovereigns should, until further notice, be received as equivalent to 10 rupees and 5 rupees respectively, in payment of sums due to Government. In the following March, the directors of the Bank of Bengal‡ urged that, "in view of the continued influx of sovereigns," the time had come when British gold might, "with safety and advantage, be declared legal tender at the respective rates of ten and five rupees," and the Government of India again pressed their original proposal on the Imperial Government. The Secretary of State replied on 17th May 1865, that the time did not appear to have arrived for taking any further step, nor did he see that any practical advantage would attend the proposal to admit British gold to legal tender in India. On 28th October 1868, the Government of India raised the rate for the receipt of sovereigns and half-sovereigns at the public treasuries from Rs. 10 and Rs. 5 to Rs. 10¼ and Rs. 5⅛, respectively.

* H. of C., No. 152 of 1858.
† H. of C., No. 79 of 1865.
‡ H. of C., No. 368 of 1865.

7. In 1876,* after the rupee had temporarily fallen in exchange to $18\frac{1}{2}d.$, the Bengal Chamber of Commerce and the Calcutta Trades' Association urged the temporary suspension of the compulsory coinage of silver by the Indian mints. The Government of India decided that "up to the present there is no sufficient ground for interfering with the standard of value."

8. In 1878,† however, the Government of India expressed a different opinion, being "led to the general conclusion that it will be practicable, without present injury to the community as a whole, or risk of future difficulties, to adopt a gold standard while retaining the present silver currency of India, and that we may thereby in the future fully protect ourselves from the very real and serious dangers impending over us so long as the present system is maintained." Aiming at the eventual adoption of the British standard, and the extension to India of the use of British gold coins, the Government proposed to proceed at the outset as follows: "We first take power to receive British or British Indian gold coin in payment for any demands of the Government, at rates to be fixed from time to time by the Government, till the exchange" (about 1*s.* 7*d.* in 1878) "has settled itself sufficiently to enable us to fix the rupee value in relation to the pound sterling permanently at 2*s.* Simultaneously with this, the seignorage on the coinage of silver would be raised to such a rate as would virtually make the cost of a rupee—to persons importing bullion—equal in amount to the value given to the rupee in comparison with the gold coins above spoken of. We should thus obtain a self-acting system under which silver would be admitted for coinage at the fixed gold rate as the wants of the country required; while a certain limited scope would be given for the introduction and use of gold coin, so far as it was found convenient or profitable." The above proposals of 1878 were referred to a Departmental Committee, who, on 30th April 1879, briefly reported‡ that they were "unanimously of opinion that they cannot recommend them for the sanction of Her Majesty's Government." A discussion of some of the reasons which appear to have influenced the Committee of 1879 in urging the rejection of the proposals referred to them will be found in the evidence given before us by Sir Robert Giffen, who was a member of that Committee. (*See* Questions 10,025-48.)

9. Between 1878 and 1892 the continued fall in the gold price of silver caused repeated embarrassment to the Government of India; but the main object of such attempts as were made by that Government to deal with the subject during the period in question was not to effect a change of standard in India, but to facilitate an international agreement which might cause a rise in the gold-price of silver, and thus diminish the inconvenience resulting from the retention of a silver standard in India.

* H. of C., No. 449 of 1893.
† C.—4868 of 1886.
‡ C.—4868 of 1886, p. 26.

10. In 1881 Indian delegates were sent to the Monetary Conference at Paris, with instructions that "while the Secretary of State in Council is unwilling to encourage an expectation of any material change at present in the monetary policy of India, he would be ready to consider any measures . . . calculated to promote the re-establishment of the value of silver."* In 1886, shortly before the appointment of the Royal Commission on Gold and Silver, the Government of India expressed the opinion that "the interests of British India imperatively demand that a determined effort should be made to settle the silver question by international agreement;"† and in 1892 Indian representatives were sent to the International Monetary Conference at Brussels, which was convened for the consideration of measures for the increased use of silver as currency.

11. In 1892, inasmuch as it was foreseen that the International Conference might fail to secure the objects for which it was to be called together, the idea of changing the standard of value in India from silver to gold had been once more brought into prominence by the action of the representatives of the mercantile community of Calcutta. On 18th February 1892,‡ when the International Conference was in prospect, the Bengal Chamber of Commerce represented that it was "impossible for men of business to feel any confidence in the future value of the rupee, and they believe that such a state of things restricts the investment of capital in this country and seriously hampers legitimate enterprise." If success could not be secured by International Agreement, the Chamber saw nothing "but the prospect of endless fluctuations in the relative values of silver and gold, attended with a fall in the value of silver of indefinite amount; and the Committee [of the Chamber of Commerce] think that in such case the Government of India should take steps to have the question of the advisability of introducing a gold standard into India carefully and seriously considered by competent authorities." In their Despatch of 23rd March 1892, the Government of India, while urging the Secretary of State to lend his "support to any proposals that might be made by the United States of America, or by any other country, for the settlement of the silver question by international agreement," called attention to the probability that, failing an international agreement, the United States would be forced to stop the purchase and coinage of silver; and they requested the Imperial Government, in view of this contingency, to take forthwith into consideration whether any, and, if so, what measures could be adopted for the protection of Indian interests. On 21st June 1892, the Government of India proceeded to record their "deliberate opinion that, if it becomes evident that the International Conference is unlikely to arrive at a satisfactory conclusion, and if a direct agreement between India and the

* H. of C., No. 449 of 1881.
† C.—4868 of 1886. *See also* First Report of Gold and Silver Commission, pp. 353—9.
‡ C.—7060, II of 1893, p. 145 *et seqq.*

United States is found to be unattainable, the Government of India should at once close its mints to the free coinage of silver and make arrangements for the introduction of a gold standard." In a telegram of 22nd January 1893,* the Government of India further explained their proposals, as follows:—"Our proposal is that we shall take power to issue a notification declaring that English gold coins shall be legal tender in India at a rate of not less than $13\frac{1}{3}$ rupees for one sovereign [*i.e.*, 18*d.* per rupee]. . . . An interval of time, of which the length cannot be determined beforehand, should, we think, elapse between the mints being closed and any attempt being made to coin gold in India. The power to admit sovereigns as legal tender might be of use as a measure *ad interim*, but it need not be put into force except in case of necessity."

12. The proposals of the Government of India were referred on 21st October 1892 by the Earl of Kimberley, then Secretary of State for India, to a Committee consisting of the late Lord Herschell, Lords Farrer and Welby, Mr. Leonard Courtney, Sir Arthur Godley, Lieutenant-General Sir Richard Strachey, and the late Mr. Bertram Currie; and on 31st May 1893 (the Brussels Conference having meanwhile adjourned without arriving at any agreement), the Committee reported as follows:—†

"While conscious of the gravity of the suggestion, we cannot, in view of the serious evils with which the Government of India may at any time be confronted if matters are left as they are, advise your Lordship to overrule the proposals for the closing of the mints and the adoption of a gold standard, which that Government, with their responsibility and deep interest in the success of the measures suggested, have submitted to you.

"But we consider that the following modifications of these proposals are advisable. The closing of the mints against the free coinage of silver should be accompanied by an announcement that, though closed to the public, they will be used by Government for the coinage of rupees in exchange for gold at a ratio to be then fixed, say 1*s.* 4*d.* per rupee; and that at the Government treasuries gold will be received in satisfaction of public dues at the same ratio.

"We do not feel ourselves able to indicate any special time or contingency when action should be taken. It has been seen that the difficulties to be dealt with have become continually greater: that a deficit has been already created, and an increase of that deficit is threatened; that there are at the present moment peculiar grounds for apprehension; and that the apprehended dangers may become real with little notice. It may also happen that, if action is delayed until these are realised, and if no step is taken by the Indian Government to anticipate them, the difficulty of acting with effect will be made greater by the delay. It is obvious that nothing should be done prematurely or without full deliberation;

* C.—7060, II of 1893, p. 183.
† C.—7060 of 1893, p. 18.

but, having in view these considerations, we think that it should be in the discretion of the Government of India, with the approval of the Secretary of State in Council, to take the requisite steps, if and when it appears to them and to him necessary to do so."

13. The Committee's recommendations having been approved by the Imperial and Indian Governments, there was passed, on 26th June 1893,* the Act, No. VIII of 1893, "to amend the Indian Coinage Act, 1870, and the Indian Paper Currency Act, 1882." This Act provided for the closing of the Indian Mints to the "free coinage" of both gold and silver—Government retaining the power to coin silver rupees on its own account. By Notifications (Nos. 2662-4) of 26th June 1893, arrangements were made (*i*) for the receipt of gold at the Indian Mints in exchange for rupees at a rate of 16*d*. per rupee, (*ii*) for the receipt of sovereigns and half-sovereigns in payment of sums due to Government at the rate of Rs. 15 for a sovereign, and (*iii*) for the issue of Currency Notes to the Comptroller-General in exchange either for British gold at the above rates or for gold bullion at a corresponding rate.

14. In 1897 the Secretary of State for India referred to the Government of India the question whether, if the Mints of France and the United States of America were opened to the free coinage of silver as well as gold at a ratio of 15½ to 1, the Government of India would undertake to re-open concurrently the Indian Mints to the free coinage of silver and to repeal the above Notifications of 1893. In reply, the Government of India expressed their "unanimous and decided opinion" that it would be "most unwise to re-open the Mints as part of the proposed arrangements, especially at a time when we are to all appearance approaching the attainment of stability in exchange by the operation of our own isolated and independent action."† This conclusion was endorsed by the Secretary of State for India in Council and by the Imperial Government.

15. In January 1898, "in order to afford a means of relief to the severe stringency" then prevailing in the Indian money markets, an Act was passed (No. II of 1898),‡ empowering the Government of India to direct, by Order notified in the Gazette of India, the issue of Currency Notes in India on the security of gold received in England by the Secretary of State at the rate and subject to the conditions to be fixed by such Order. Under this Act, which was to remain in force for six months, a Notification was published by the Government of India on the 21st January 1898, announcing that notes would be issued, in exchange for gold held by the Secretary of State for India, at the rate of one Government rupee for 7·53344 grains of fine gold, with the addition of such further quantity of fine gold as the Secretary of State should from time to time determine to be

* C.—7098 of 1893.
† C.—8867.
‡ See Appendix, p. 34.

"sufficient to cover all costs and charges incidental to the transmission of gold to India." Under this Notification, the Secretary of State in Council gave notice of his readiness "to sell, until further notice, telegraphic transfers on Calcutta, Madras, and Bombay, at a rate not exceeding 1*s.* $4\frac{5}{32}$*d.* for the rupee." This Act was extended for a further period of two years by the amending Act, No. VIII of 1898. No gold has been tendered under the provisions of these Acts.

16. It will thus be observed that, at the present time, gold is not a legal tender in India, though the Government will receive it in the payment of public dues; that the rupee remains by law the only coin in which other than small payments can be made; that there is no legal relation between rupees and gold; but that the Indian Government has declared (until further notice) a rate at which rupees can be purchased for gold coin or bullion—such rate serving to determine the maximum limit to which the sterling exchange can rise under present arrangements.

II

A Silver Standard.

17. Having thus set forth the origin and present position of the monetary system of India, we proceed to consider the question whether, in the light of the six years' experience gained since 1893, it is desirable to reverse the policy initiated in that year and to re-open the Indian mints to the unrestricted coinage of silver. Such a step has not been advocated in the Memorials which we have received from the Chambers of Commerce of Bengal, Bombay, Madras and Karachi.* Nor is there unanimity among those who do advocate so important a change of policy. Apart altogether from the fact disclosed by the evidence that some who were opposed to the closing in 1893, now advocate a gold standard, there is a clearly marked division between those who would re-open the mints to silver forthwith and those who, while contemplating such a course eventually, hesitate to re-open the mints immediately. The latter class may be further subdivided into those who propose to leave the time and conditions of such re-opening to be hereafter determined, and those who suggest immediate steps towards a gradual re-opening. With regard to the last suggestion, which aims at mitigating what its advocates have represented to us as the prospects of disaster to merchants and traders and of grave difficulty to the Government of India from the sudden drop in exchange to the bullion value of the rupee (about $10\frac{1}{2}$*d.* at the present time), no scheme has been submitted to us which appears likely to attain the object in view. In our opinion, any measures for gradual re-opening would be so fully and immediately discounted as to defeat the

VSC * *See* Appendix, p. 17 *et seqq.*

precise objects for which they are suggested. It is obvious, moreover, that the certain prospect of a heavy fall in the exchange would at once drive capital from India.

18. As regards the policy which, while declaring in favour of open mints, would leave it to future undefined circumstances to indicate when the step should be taken, this (so far as it is not dictated by the desire for an international agreement, to which we refer presently) recognises that, for the present, the benefits anticipated from a return to a silver standard do not counterbalance the evils which would result from abandoning the *status quo*. The hope apparently is that, from a rise in the gold-price of silver, or from a fall in the sterling exchange of the rupee, or from a combination of these or other undefined circumstances, it may hereafter become possible to revert to a silver standard without causing a sudden and heavy fall in the exchange value of the rupee. Meantime it is proposed that the present arrangements should continue indefinitely, in spite of the disabilities considered to be thereby imposed on what are regarded as the true interests of India. This suggestion could, of course, only be entertained by the Government of India if it were definitely decided, in principle, to re-open the Indian mints to silver; and its adoption or rejection must depend on the answer to the broad question with which we are about to deal, *viz.*:—Is it desirable for India to revert to silver monometallism?

19. The policy of re-opening the mints at some future date to silver stands on a different footing when urged by those who look forward to an international agreement and consider that there is reasonable hope of such an agreement within a limited period. Such persons, unlike those above referred to, aim directly at a stable exchange between India and the United Kingdom, and advocate delay only in order that an international agreement may be reached. With regard to this anticipation, we confine ourselves here to stating that, the negotiations of 1897 with France and the United States of America having proved fruitless, no fresh proposals, so far as we are aware, have been, or are being, made by any of the Governments concerned.

20. The main proposal that the Indian mints should be reopened forthwith to the unrestricted coinage of silver has been supported by witnesses on various considerations, one of which is that "a low rupee and a low exchange" encourage the export trade on which India's prosperity depends, and that an "arbitrarily enhanced" rupee discourages exports. It is urged that encouragement would best be given to exports by a reversion to the system of open mints, so that the rupee in exchange would again coincide with the gold price of silver, with the result that an end would be put to the unfair advantage which the present system is held to give to the silver-using competitors of India, and which (according to this view) the effective establishment of a gold standard would perpetuate. Great stress is laid by the advocates of open mints upon the burthen imposed on the

export trade of India by stringency in the Indian money market, which they attribute to the closing of the mints, and represent as likely to increase under the present system of closed mints. It is admitted generally by the advocates of open mints that the benefits which would accrue to India from restoring the silver standard would probably lead to difficulties on the part of the Indian Government; but it is urged that these difficulties would be temporary only, and that they could be met either by borrowing or by increased taxation, including import and export duties.

21. Dealing first with the question of discount rates, it will be sufficient to remark that the anticipations of increasing stringency have not been verified during the recent busy season. Whereas the minimum rate of the Bank of Bengal was 10 per cent. on 6th January 1898, rising on 24th February to 12 per cent. (at which figure it stood until 27th April 1898), and did not fall below 10 per cent. until 16th June 1898, the rate for the busy season of 1898-99 has never exceeded 7 per cent., and this though the total volume of India's seaborne foreign trade exceeded Rx. 210,000,000 in 1898-99, as against (under) Rx. 199,000,000 in 1897-98.

22. While it may be questioned whether banking arrangements in India might not with advantage be strengthened and adjusted to the growing requirements of Indian trade, we cannot doubt that one of the main causes of the stringency of 1897-98 was the reversal (necessitated by the exceptional circumstances of India at the time) of the relations of the Government of India and the money market in the autumn of 1897. In ordinary years the Government is able, through the sale of Council Bills and Telegraphic Transfers, to place large sums at the disposal of the money market throughout the autumn and winter. Thus, during the last months of 1894, the bills and transfers sold by the Secretary of State amounted to Rx. 8,052,000; in 1895, for the same period of the year, the amount was Rx. 9,888,000; in 1896 the amount was Rx. 6,056,900. But in 1897, owing to the depletion of the balances of the Government of India, brought about by expenditure on famine relief and military operations and by failing revenue, the Secretary of State was unable, from 1st September to 15th November, to offer bills or transfers for sale, and was compelled to purchase drafts on India for Rx. 1,000,000. Thus, during the last four months of 1897, the amount placed at the disposal of the Indian money market in the Presidency towns in consequence of the remittance transactions of the Government was only Rx. 332,700, or Rx. 5,724,200 less than the year before.

23. It must not be forgotten that high discount rates were not unknown in India under the system of open mints; for example, the Bank rate reached 12 per cent. in April 1890 (in which year the rate did not fall below 10 per cent. from 10th February to 24th April), while in 1889 12 per cent. was quoted continuously from 21st February to 28th March, the rate not falling below 10 per cent. from 17th January to 11th April of that year.

24. We come next to the suggestion that the present system of closed mints handicaps India in her industrial competition with countries on a silver standard.

Of such countries China may be taken as the type, and it is said that the greater fall in (say) the London exchange with China as compared with the fall in the exchange with India stimulates exports from China which compete with exports from India, and also stimulates native production in China to the disadvantage of Indian imports into China; and that in this way India is placed at a disadvantage, and that the disadvantage to India is increased when an actual rise occurs in the Indian exchange.

It is explained that a fall in the price of silver is necessarily accompanied by a fall in the China exchange, that the producer in China consequently receives a higher silver price in respect of the same gold price, whilst wages and the other factors in the cost of production do not increase in the same proportion; that production in China becomes more profitable and is therefore stimulated; that, on the other hand, if the Indian exchange does not fall to an equal degree, the Indian producer does not receive this stimulus, and, if the Indian exchange rises, the producer in that country receives a lower rupee price, while wages and the other factors in the cost of production do not proportionately diminish; that the Indian producer does not receive the same profit as before, and that production is therefore checked.

This aspect of the question was considered by Lord Herschell's Committee, and the conclusions at which they arrived will be found in paragraph 27 of their Report. They expressed the opinion that, even if we assume the argument as to a stimulus or check to production to be sound, the effect of each successive fall in exchange must be transitory, and could only continue until circumstances have brought about the inevitable adjustment. In this opinion we concur, and evidence has been laid before us which shows that prices and wages have risen in China since silver has fallen in price and the local copper currency has appreciated in terms of silver.

25. Lord Herschell's Committee examined the statistics of Indian exports for a series of years, and came to the conclusion that "although one may be inclined, regarding the matter theoretically, to accept the proposition that the suggested stimulus would be the result of a falling exchange, an examination of the statistics of exported produce" [from India] "does not appear to afford any substantial foundation for the view that in practice this stimulus, assuming it to have existed, has had any prevailing effect on the course of trade; on the contrary, the progress of the export trade has been less with a rapidly falling than with a steady exchange."

We need not quote the statistics of the export trade to which that Committee called attention, but we desire to state that we have been unable to find any statistical support for the theory

that exports are largely and permanently stimulated by a depreciation of the standard of value, resulting in a fall in the exchange.

The statistics of the Indian export trade since the mints were closed to silver might have been expected to throw light on this portion of the question, but their value for this purpose is much diminished by the special disturbing influences to which that trade has been subjected during the last six years.

The closing of the Indian mints, the cessation of the purchases of silver by the United States of America, the consequent fall in the price of silver, and the apprehension to which it gave rise, undoubtedly disturbed the course of trade for a time, and when recovery to more normal conditions might have been expected, India was affected by war, famine, and plague, and its finances were so seriously embarrassed that the drawings of the Secretary of State were largely reduced, and loans of unusual magnitude were raised in London on account of the Government of India. The exports from India were largely reduced in 1897-98. In the following year (1898-99) there was a marked recovery; the drawings by the Secretary of State were unusually large; and a substantial sum in gold was brought to the Indian Treasury.

26. For convenience of reference we give in this place the figures of gross exports from India in the 12 years from 1887-88 to 1898-99.

Year.	Exchange.	Silver, per oz.	Exports of Merchandise.
	d.	*d.*	Rx. (000 omitted).
1887—88	16·898	$44\frac{5}{8}$	90,471
1888—89	16·379	$42\frac{7}{8}$	96,978
1889—90	16·566	$42\frac{11}{16}$	103,397
1890—91	18·089	$47\frac{11}{16}$	100 136
1891—92	16·733	$45\frac{1}{16}$	108,036
1892—93	14·985	$39\frac{13}{16}$	106,536
1893—94	14·547	$35\frac{5}{16}$	106,448
1894—95	13·101	$28\frac{15}{16}$	108,815
1895—96	13·638	$29\frac{7}{8}$	114,263
1896—97*	14·451	$30\frac{3}{4}$	103,914
1897—98*	15·354	$27\frac{9}{16}$	97,597
1898—99	15·978	$26\frac{15}{16}$	112,723

* Famine years.

For the reasons we have stated in the preceding paragraph, we hesitate to draw any positive conclusion from these figures, but they afford no support to the theory that large exports are incompatible with a rise in the rate of exchange.

27. In this connexion we wish specially to notice the very important Tea Industry of India and Ceylon, which certain witnesses stated to be seriously threatened by competition with China tea produced in a country on a silver basis. We recognise the large capital invested in the tea estates, and that their maintenance is of vital importance to the many Europeans and natives employed therein. It was represented to us that the profits of the producers of Indian and Ceylon tea had been affected by the recent rise in the Indian exchange; that although this diminution of profit could not immediately affect the total export of tea from gardens already in existence, or the increase from gardens in process of formation and about to come into bearing, it would tend to diminish the extension of cultivation, and thus prevent the export of tea from increasing to the extent to which it would otherwise have done.

We do not doubt that the recent rise in the Indian exchange temporarily diminished the profits of the producers of tea, just as the previous fall had temporarily increased them; but, as we have already said, we see no reason to suppose that the strength of the competition of China tea will be permanently increased by the fact that China is on a silver basis. So far there is no evidence to show that the exports of China tea have appreciably increased, and there is evidence to show that the rise in Chinese wages and general prices has at least begun to take effect.

It appears to us that the permanent interests of the tea gardens of Ceylon and India will be promoted rather than injured when their operations are carried on under the same standard of value as exists in the countries to which their produce is exported.

We find that this question of the competition of China with Indian tea was specially considered by the Government of India in 1892, before the Indian mints were closed to silver, in connexion with a memorial on the subject from the Darjeeling Planters' Association. The views of the Government of India on the subject are contained in a letter to the Honorary Secretary to the Association, dated 12th October 1892, and printed at pages 176-77 of the Minutes of Evidence before Lord Herschell's Committee. The following extract from that letter contains a summary of the views which the Government of India expressed at that time:—

"To sum up, the Government of India are of opinion—

(1) That a country, as a whole, makes no gain in its international trade by a depreciation of its standard, since the extra price received for its exports is balanced by the extra price paid for its imports.

(2) That the producer of an article of export may make a temporary and unfair gain from depreciation of the standard, at the expense of his employés and of other persons to whom he makes fixed payments.

(3) But that this gain, while not permanent, is counterbalanced by a tendency to over-production and consequent reaction and depression, by a liability to sudden falls in price as well as to rises, and by the check to the general increase of international trade which necessarily results from the want of a common standard of value between countries which have intimate commercial and financial relations."

We are unable to find that anything has occurred since the closing of the Indian mints to silver to throw doubt on the soundness of the views expressed in 1892 by the Government of India.

28. As regards the argument that a low exchange stimulates exports and discourages imports, it is further to be observed that whatever advantages attach to a low exchange should be increased, by parity of reasoning, by a still lower exchange; and it has accordingly been represented to us that it is a falling exchange which stimulates exports. But, as regards the ultimate limits of beneficial fall, we have failed to discover at what precise point, if at all, the advocates of this view would hold that the alleged advantages of a falling exchange cease.

29. To re-open the Indian Mints to silver without an international agreement would necessarily result, according to all past experience, in renewed instability of the exchanges between India and gold-standard countries. It is generally recognized that fluctuations of exchange constitute an obstacle to international trade, the true interests of which are to be sought in a stable monetary par of exchange. Since over four-fifths of India's seaborne foreign trade is with gold-standard countries, it follows that the balance of advantage is heavily in favour of stability of exchange with gold-standard countries; and accordingly, considered by itself, the instability of exchange which must be anticipated from re-opening the Indian Mints to silver, is a powerful argument against taking the step.

30. So far we have considered the matter solely from the standpoint of trade; and the above remarks will have indicated our conclusion that, even apart from considerations primarily affecting the Government of India, it is not in the permanent interests of India that her foreign commerce, over 80 per cent. of which is with gold-standard countries, should be hampered by the restorations of silver monometallism. This conclusion is strengthened by considerations affecting the Government of India, which is the representative of the general interests of India. Apart from certain large payments in India (such as the pay of British soldiers serving in that country), the rupee total of which payments is regulated by the sterling exchange, the Secretary of State for India has

now, under normal conditions, to meet obligations in England amounting annually to between 17 and 18 millions sterling. In order to make these payments, the Government of India raises taxation in rupees, and would therefore be seriously affected by the re-opening of the mints to silver. It is impossible to foretell what would be the actual effects of this step on exchange. But a drop even to 1*s*. (which is about 2*d*. above the present bullion value of the rupee) would, on a moderate estimate, increase the necessities of the Government of India by at least Rx. 10,000,000 gross, against which might be set some possible increase of revenue, leaving an increase of at least Rx. 7,000,000. This sum exceeds the total excise revenue of India by Rx. 1,500,000, exceeds the total stamp revenue by Rx. 2,160,000, and is nearly four times the total yield of the Indian income tax. An increase of expenditure to this extent would not only absorb the whole of the present surplus—which is the result of an increase in taxation imposed since 1886 principally to meet exchange difficulties—but would also necessitate further taxation. As regards an increase of taxation, Lord Northbrook has expressed the opinion (Q. 8,407) that, while it would be possible, " it would be in the highest degree unwise, both in respect of the trade of India, the welfare of the people of India, and I will go far as to say the security of the Indian Empire." Concurring as we do in this opinion, which has been supported by the independent testimony of other distinguished administrators of India, we must add that the Government of India would not be justified in assuming that, with the mints re-opened to silver, the fall of the exchange to a shilling is the greatest fall which they might be called upon to face either immediately or at a future time.

31. It has been urged before us that, so long as the rupee is current at a value considerably above that of the silver which it contains, there is serious risk of counterfeit coins in silver of standard fineness being manufactured and put into circulation. This subject has engaged the attention of the Government of India; and in a despatch dated 12th January 1899 (more than five and a half years after the closing of the mints), they express the opinion that there is no evidence of such counterfeiting on any appreciable scale. We see no reason to doubt the correctness of that opinion; nor does the experience of other countries, in which silver coins circulate at an enhanced value, suggest any other conclusion.

32. In view of the considerations which we have stated, we concur with the Government of India in their decision " not to revert to the silver standard."

III.

The Principle of a Gold Standard.

33. At the present time, the practical alternative to silver monometallism is a gold-standard, that is to say, gold as the

measure of value in India, either with a gold currency or with a gold reserve.

34. We have already referred to the fact that over four-fifths of the foreign trade of India is with gold-standard countries, and that for this reason it is desirable that India should have the same measure of value as those countries. Regard being had to the supremacy of gold in international commerce, the change to a gold basis has been represented to us by Professor Marshall (Q. 11,815) as "*like a movement towards bringing the railway gauge on the side branches of the world's railways into unison with the main lines.*" This consideration directly relates to facilitating interchange of commodities.

35. A further and certainly not a less important consideration for a country like India is that an established gold-standard is the simplest and most effective means of attracting capital. The need of India for foreign capital is indisputable, and this need is partly of a temporary and partly of a permanent character. For climatic reasons, India is essentially a country of seasonal trade; she has a busy season and a dull season, though the tendency of late years has been to diminish the disparity and to exhibit approximation to a more uniform average within each year. From this seasonal character it follows that the demand for money is much greater for one part of the year than for the other. In the busy season there is a brisk demand for temporary advances to move the crops; in the dull season money is in little demand. The distinction is shown in an extreme form by the facts of the money market in 1897-8, when there was a seasonal variation in discount rates of no less than 7 per cent., and the fluctuations were even greater in 1889 and 1890. In order to diminish the risk to Indian commerce of a recurrence of such stringency, and in order to reduce the average rate charge for the local use of money, the sound policy is to attract capital to India from the gold-standard countries which have capital to lend, and this can best be achieved by a gold standard and a stable exchange. Moreover, it is in many ways as important that money should be able to flow out of a country without depreciation, when it is no longer in relative demand there, as that it should flow in when required. A gold standard is, in our opinion, the only means by which, under present conditions, these benefits can be secured.

36. The natural resources of India are beyond question, as also is the need for their development. In order to develope and reap the benefit of her resources, India requires, and must long continue to require, foreign capital. Such foreign capital can only be drawn from the gold-standard countries; and the capital of these countries can only be attracted by a moderate rate of interest or profit on condition that the investor is satisfied that there is not likely to be a fall in the sterling exchange. We have had the valuable testimony of Mr. Alfred de Rothschild (Q. 11853) that British capital would be at once forthcoming if the British investor

knew that there was a fixed rate of exchange between the two countries. We attach great importance to this argument in favour of a gold standard for India.

37. It seems unnecessary to discuss the further considerations which point to the benefits to India of a gold standard. We desire, however, to remark that the effective establishment of such a standard in India would not preclude India hereafter from considering responsible proposals for an international agreement, if circumstances should arise to render such negotiations practicable.

38. Before discussing the various further measures which have been proposed for establishing a gold standard in India, we submit to your Lordship the following considerations relating to the existing currency arrangements. Inasmuch as, for practical purposes, the sterling exchange furnishes a broad test of a country's claim to be on a gold standard, and inasmuch as the Indian exchange since January 1898 has been stable (within what may be regarded as "specie points") at 16*d.* per rupee, it has been represented to us that the gold standard may be regarded as having been reached in India already. According to this view, the closing of the Indian mints to silver and the undertaking by the Government to give rupees for gold has already had the result of making gold practically a legal tender in India, present arrangements being sufficient to supplement automatically from time to time the stock of currency.

39. Judged solely by existing facts, this contention cannot be disputed in its essentials. Events have proved more favourable than was anticipated by the Government of India when, in their despatch of 3rd March 1898, they represented that it was not very probable that gold would be presented in the early future. And, although they expressed the opinion that it was "in any case extremely unlikely to be presented in such quantity as to lead automatically to an accumulation of gold sufficient for a reserve," statistics indicate that a considerable accumulation has already been effected. On 31st March 1899, the reserve of the Paper Currency Department of the Government of India included gold to the amount of over 2,000,000*l.* sterling. At the present time the amount of gold is 2,378,609*l.*

40. While this substantial addition in gold was being made to the Indian currency, the Government of India was able, within the year to 31st March 1899, to remit by the sale of Council Bills a sum of 18,712,454*l.*, which is considerably more than the average sterling requirements of the Secretary of State, and was 2,712,454*l.* in excess of the orginal estimate of his sterling drawings. This has been accomplished without lowering the average price realized by the sale of Council Bills below 15·978*d.* (or as nearly as possible the limit fixed in 1893); and stringency has not recurred in the money-market. Automatically, therefore, existing currency arrangements sufficed not only to maintain—without monetary stringency—a steady gold standard in 1898-9, but also to

initiate a gold reserve in India, to serve as a bulwark for the maintenance of the gold standard in future years.

41. If it has been possible to secure these results in the past in the face of distrust, it may be argued that even greater success may be expected in the future with the growth of confidence. We are by no means prepared to suggest that this may not prove the case, or that the mere continuance of the *status quo* may not prove adequate by itself gradually to supplement the currency of India with a margin of gold sufficient to tide her over adverse years hereafter. But the same considerations which tell in favour of maintaining the *status quo* for the present, equally tell against its maintenance permanently. In practice it would be impossible for the Government of India to receive gold beyond a certain point into their Treasuries or their Paper Currency reserve, unless they were also empowered to pay that gold out again in cashing their notes or meeting other liabilities in India. But this would mean declaring gold a legal tender at a fixed rate, and thereby superseding the purely provisional machinery of the existing system. According to this argument, therefore, maintenance of the existing system comes to mean little more than postponing further action for a time. The interval would be long or short, according to the slow or rapid accumulation of gold; but in no case could the provisional arrangements now in force constitute—nor indeed, were they ever intended to constitute—a permanent settlement of the problem. The practical question is, therefore, narrowed to this:—Should the *status quo* be allowed to continue until events force the Government to take action? There would have been more to be said in favour of suspending action and leaving facts to settle the problem, had it not been for the circumstances which led the Government of India to formulate proposals for curtailing the transition period and taking "active steps to secure the early establishment of a gold standard and a stable exchange." That opinion having been expressed by the Government of India, and public discussion having been aroused by the publication of their proposals and by the present inquiry, it appears to us undesirable, even though results have proved more immediately successful than the Government of India anticipated on 3rd March 1898, to leave matters as they are. If, in face of the public attention which the question has attracted, and in face of the considerable divergence of the views expressed on the subject, no further steps were now to be taken, an additional uncertainty would be caused; doubts would be excited as to the ultimate success of the gold-standard; rumours would arise of a possible change of currency policy; the Government both in India and at home would be pressed for a final pronouncement, alike by the friends and by the foes of a gold standard: and meantime the material interests of India would suffer from the withdrawal of confidence in her monetary future.

For these reasons we conclude that steps should be taken to avoid all possibility of doubt as to the determination not to revert to a silver standard, but to proceed with measures for the effective establishment of a gold standard.

IV.

The Indian Government's Proposals.

42. Having thus expressed our agreement in the objects which the Government of India have in view, we pass to the consideration of the specific measures proposed by them with a view to making effective the monetary policy adopted by Her Majesty's Government in 1893 and initiated by the closing of the Indian Mints to the unrestricted coinage of silver.

43. The proposals of the Indian Government were contained in their despatch of 3rd March 1898, and have been explained to us by official witnesses. They may be summarised as follows:—

In order to keep the exchange value of the rupee at a steady level of 16*d.*, it was deemed necessary to decrease the rupee circulation so as to remove the relative redundancy. The amount to be so withdrawn could not be foretold with exactness, but it was more than probable that it would fall short of Rx. 24,000,000. Within this outside limit it was proposed "to melt down existing rupees, having first provided a reserve of gold, both for the practical purpose of taking the place of the silver, and in order to establish confidence in the issue of our measures." The first step was to take powers to borrow sums not exceeding in the whole 20,000,000*l.*, and at once to remit 5,000,000*l.* in sovereigns to India as a first instalment. If exchange remained at or above 16*d.*, there would be no further step [Q. 2653]. But if, and so long as, the exchange fell below 16*d.* [Q. 2657-8], the Government of India would take rupees from its balances, melt them down, sell the bullion for other rupees in India (at an assumed loss of 40 per cent.), pay these other rupees into its balances, and finally make good thereto the 40 per cent. balance of loss with part of the borrowed gold. It was anticipated [Q. 2663] that one borrowing (5,000,000*l.*) might be sufficient, that sum approximately covering the assumed loss to Government of Rx. 8,000,000 on melting down Rx. 20,000,000. As a result, it was anticipated that by the automatic operations of trade, gold would flow into the country and remain in the circulation. But until the exchange value of the rupee was established at 16*d.*, and sovereigns became, to some extent however small, a permanent part of the circulation, it was not the Government's intention to part with any of the gold in their possession. Meantime, gold was not to be made a legal tender in India, though the Government looked forward to this as a future goal.

44. The proposals of the Government of India were based on the belief that the rise in the value of the rupee, and in the exchange with London, subsequent to the year 1894-5, was due to a contraction of the Indian currency relative to the demands of trade, that this cause would continue to operate so long as the Indian Mints were closed to silver, and that, if only that stage of distrust could be passed, "which appears the moment exchange

approximates to sixteen pence to bring into operation influences which interfere with the actual realisation of that rate," the exchange, under normal conditions of trade, might be expected "to attain the level at which gold would be tendered under the notification of 26th June 1893, and the introduction of the gold standard would become practicable."

They were anxious "both in the interests of the State and of the mercantile community to terminate the period of transition without further delay,"—in the interests of the State, because it would be cheaper in the end to acquire a reserve of gold by borrowing, and thus keep the exchange value of the rupee at a steady level of sixteen pence than to bear for years the burden of expenditure entailed by the lower level of the rupee; in the interests of the commercial community, because it was not desirable that their legitimate business should be hampered and embarrassed by the uncertainty of exchange, while the want of confidence in the stability of the rupee discouraged the investment of capital in India, and available capital was remitted to England whenever the exchange value of the rupee rose to a high level.

The proposals of the Government of India were made in March 1898, and since that date there has been a marked improvement in the position. The exchange has been steady at or about 1*s.* 4*d.*, the drawings of the Secretary of State have been unusually large, and a substantial sum of over 2,370,000*l.* in gold has been brought to the Indian Treasury; in other words, what the Government of India described as the "stage of distrust," which interfered with the actual realisation of a rate of sixteen pence, has been already passed.

If the Government of India could have foreseen the course of events in the past year, it is possible that their recommendations might not have taken the precise form in which they were put forward; and we are informed that, even if their proposals had been sanctioned at once, they would not under the conditions that have since prevailed have given effect to that portion of their scheme which provided for the withdrawal of rupees from the Indian currency. However that may be, we think it desirable that the proposals of the Government of India should, even under the altered conditions of the present day, be carefully considered by us.

45. In the first place we desire to point out that it has not been proved that the rise in the value of the rupee since 1894-5 is due solely to relative contraction of the Indian currency; and it may be that it is not due mainly to this cause. It is not certain that there has been any contraction of the Indian currency which has materially affected the exchange, though it may not unreasonably be inferred that there must have been some contraction, and that such contraction has had some influence on the exchange value of the rupee. On the other hand, there are causes other than contraction of the currency which affect the value of the rupee and the exchange with London. Large borrowing in London

on account of India, reduction of the drawings of the Secretary of State, an increase in the exports from India unaccompanied by an equivalent increase in imports, as well as a general rise in gold prices, would all affect the rate of exchange with India, though it is quite impossible to estimate the relative importance of these factors among themselves, or the amount of their influence on exchange as compared with the effect of a contraction of the currency, or to state the precise degree of influence which any, or all of them, have had on any particular alteration in the exchange. Nor, on the other hand, is it certain that the unusually low rate of exchange that prevailed in 1894-5 was due solely to a relative redundancy of the Indian currency. The closing of the Indian Mints necessarily brought into play many disturbing influences which may have affected 1894-5.

Since the mints were closed there has also been large borrowing on Indian account, and there have been, in some years, large reductions below the normal amount in the public remittances from India, while fluctuations have been experienced in the foreign trade of India, due to famine and plague as well as to other causes. All these causes must at different times have affected the exchange either favourably or unfavourably.

Another influence which must have had a favourable effect on the Indian Exchange is the reduction in the imports of silver due to the closing of the mints. The average yearly net import in the three years preceding the closing of the mints was 43,133,678 ozs., of the value of Rx. 12,020,296; and, for the three years ending 1898-9, the average net import was 31,126,376 ozs., of the value of Rx. 6,103,431.

46. In face of the facts we have just stated, we are unable to accept, without qualification, the opinion that the rise in the value of the rupee since 1894-5 has been due, wholly or mainly, to a relative contraction of the Indian currency. We are not prepared to say that the contraction of the Indian currency has not been an important factor in the rise in the Indian exchange; but, so long as the facts of the case are surrounded by so much obscurity, we consider that it would be unsafe to base action of so drastic a character on this assumption.

If it be the case that the rise in the value of the rupee since 1894-5 is not due, wholly or mainly, to the relative contraction of the Indian currency, it follows that an additional contraction of that currency, produced artificially by the withdrawal of rupees in the way proposed by the Government of India, might not have so much effect in strengthening exchange as the Government of India believed; and, though we accept in principle the proposition that a reduction in the number of rupees tends to increase the value of the rupee, we are not prepared to admit that such effect must necessarily be direct and immediate; nor are we satisfied that such reduction carried out on a large scale and within a limited period, might not aggravate, if it did not produce, a period of stringency in the Indian money market.

47. So far as the proposals of the Government of India were intended to secure the confidence of the commercial community, they have failed in their effect; these proposals have not been supported before us by the representatives of the commercial and financial interests connected with India, nor, indeed, by any of the independent witnesses whom we have examined. The commercial classes of India appear to have feared that the withdrawal of rupees from the currency would inevitably aggravate or produce stringency in the Indian money market, and that the sale of silver by the Indian Government would lower the price of that metal, and disturb the exchanges with China and other countries on a silver basis.

The argument of the Government of India that the adoption of their proposals would involve less loss to the Indian Exchequer than the maintenance of the *status quo*, does not appear to us to possess much force. If the principle on which they based their proposals was sound, namely, that the rise in exchange was due to the contraction of the Indian currency, and that the same cause would continue to act in the same direction so long as the Indian mints were closed to silver, there was no likelihood of any serious fall in exchange, and, consequently, no prospect of any considerable increase of expenditure on this account. If, on the other hand, the basis of their proposals was unsound, it was not certain that they would have produced the desired effect, and, while a considerable expenditure would have been incurred in borrowing in gold and withdrawing rupees from the currency, the operation might not have resulted in any material reduction in the charge for exchange.

Although we sympathise with the Government of India in their desire to shorten the period of transition, to inspire confidence in the commercial community, and to remove an impediment to the flow of British capital to India, and recognise the force of the pressure upon them in the beginning of 1898 to take immediate steps in a direction which, it was hoped, would lead to the desired result, we can only say that, for the reasons already stated, we do not approve of their proposals, and cannot recommend their adoption.

V.

A Gold Currency.

48. It is of greater practical importance at the present time to consider what steps the Government of India contemplated taking when, by their methods, that state of things had been established which is in actual operation to-day. They did not definitely propose to make gold coins a legal tender; but they did not hesitate to express the opinion that "the only state of things which can be called a thoroughly satisfactory attainment of a gold standard is one in which the gold coins which represent our

standard are those also which are good for payments in England." As a matter of principle, therefore, the Government of India favoured a gold standard *with* a gold currency.

49. This brings us to the consideration of schemes which have been proposed for establishing a gold standard *without* a gold currency. Great stress has been laid upon the hoarding habits of the natives of India; and, in view of the direct encouragement which a gold currency might give to the hoarding of gold, it has been represented to us by Mr. Lesley Probyn that, "if gold coins were passed into the currency, it would be at first almost like pouring water into a sieve." He accordingly proposed (*i*) to institute a separate issue of gold notes of the denomination of Rs. 10,000; (*ii*) to issue such notes only in exchange for gold; (*iii*) to make them payable (at the option of the holder) either in rupees or in gold; (*iv*) to make it optional to the Currency Department, when gold is demanded, to pay either in sovereigns or in gold bars of not less than 67*l*. It was hoped that gold would be attracted to India, and that a gold reserve would be gradually accumulated which would be strong enough to allow the Government to undertake ultimately the universal convertibility into gold of all rupees and rupee-notes, when presented in parcels of not less than Rs. 10,000. Under this scheme the gold-standard would be left to automatic agencies to establish, and its establishment would coincide with an ultimate undertaking to exchange rupee currency for gold bars of high value.

50. On this scheme we remark that, while bullion may be regarded as the international medium of exchange, there is no precedent for its permanent adoption for purposes of internal currency; nor does it accord with either European or Indian usage that the standard metal should not pass from hand to hand in the convenient form of current coin. No real support for such a scheme is to be drawn from the purely temporary provisions of "Peel's Act" of 1819, whereby, for a limited period, the Bank of England, as a first step to the resumption of cash payments, was authorised to cash, in stamped gold bars, its notes, when presented in parcels of over 200*l*. Little or no demand for gold bullion appear to have been made on the Bank under these temporary provisions, which were repealed at the instance of the Bank itself in 1821.

As regards the hoarding difficulty in India, we are not satisfied that the danger therefrom is so great as has been suggested. There is little or no likelihood, even according to the most sanguine view, that for long time to come gold coins, even if declared a legal tender forthwith, would find their way to any great extent into general circulation. Even under silver monometallism India imported and absorbed gold, as she is doing to-day, and as she may be expected to do in the future, no matter what her system of currency. In a strongly conservative country like India no sudden changes are to be expected in the habits and customs of the people, particularly in matters relating to currency and

hoarding; but, while we must look to the continuance of the habit of hoarding, we may also feel satisfied that, until gold has penetrated into general circulation (so far as the relatively small transactions of India permit), there will be no materially increased temptation to the natives of India to hoard gold instead of silver. Moreover, the introduction of a gold currency into India would not be an untried experiment. As has been shown above, gold coins were in common circulation in India generally within living memory, and were expressly stated in 1806 to form the principal currency and money of account of Madras. If hoarding did not render a gold circulation an impossibility in the past, we look for no such result in the future.

51. Consequently, we are of opinion that the habit of hoarding does not present such practical difficulties as to justify a permanent refusal to allow India to possess the normal accompaniment of a gold standard, namely, a gold currency.

52. Another plan for establishing a gold standard in India without a gold currency, was submitted and explained with great ability by Mr. A. M. Lindsay. In order to fix the sterling exchange, he proposed to make the rupee currency freely convertible in India at a fixed rate into drafts on a sterling fund located in London. At the same time rupee drafts were to be sold at a fixed rate in London. Assuming a par of 16*d.*, sterling in London was to be convertible into rupees in India at $16\frac{1}{16}$*d.*, and rupees in India were to be convertible into sterling in London at $15\frac{3}{4}$*d.*; drafts were to be sold both in India and in London to any extent; but the amount in each case was to be not less than Rs. 15,000 and 1,000*l.*, respectively. In order to provide for meeting the sterling drafts, a loan not exceeding 10,000,000*l.* was to be raised in London, while, so far as the available stock of rupees proved insufficient, silver would be purchased (also out of the loan) and sent to India to be there coined into rupees. If an excess of rupees accumulated as the result of selling sterling drafts, it might be necessary to sell the excess as bullion and credit the proceeds to the sterling fund. Under the scheme, rupees would continue to form the circulating medium of India, gold not being admitted to legal tender. While Mr. Lindsay held that such a system of currency would answer all purposes and be economical, and might, therefore, be permanently adopted, he considered [Q. 4303-4] that his scheme would be the best means of leading up to a gold currency, if this were ultimately thought desirable.

53. It is evident that the arguments which tell against the permanent adoption of Mr. Probyn's bullion scheme and in favour of a gold currency for India, tell more strongly against Mr. Lindsay's ingenious scheme for what has been termed "an exchange standard." We have been impressed by the evidence of Lord Rothschild, Sir John Lubbock, Sir Samuel Montagu, and others, that any system without a visible gold currency would be looked upon with distrust. In face of this expression of opinion, it is

difficult to avoid the conclusion that the adoption of Mr. Lindsay's scheme would check that flow of capital to India upon which her economic future so greatly depends. Moreover, if the system were to be permanent, it would base India's gold standard for all time on a few millions of gold (or rather command over gold) in London, with a liability to pay out gold in London, in exchange for rupees received in India, to an indefinite extent. This was the main reason with weighed with the Government of India in deciding not to adopt the scheme, and we think they were justified in their conclusion. We are not prepared to recommend Mr. Lindsay's scheme, or the analogous schemes proposed by the late Mr. Raphael and by Major Darwin, for adoption as a permanent arrangement; and existing circumstances do not suggest the necessity for adopting any of these schemes as a provisional measure for fixing the sterling exchange.

54. We are in favour of making the British sovereign a legal tender and a current coin in India. We also consider that, at the same time, the Indian Mints should be thrown open to the unrestricted coinage of gold on terms and conditions such as govern the three Australian Branches of the Royal Mint. The result would be that, under identical conditions, the sovereign would be coined and would circulate both at home and in India. Looking forward as we do to the effective establishment in India of a gold standard and currency based on the principles of the free inflow and outflow of gold, we recommend these measures for adoption.

VI.

Convertibility.

55. Under an effective gold standard rupees would be token coins, subsidiary to the sovereign. But existing conditions in India do not warrant the imposition of a limit on the amount for which they should constitute a legal tender; indeed, for some time to come, no such limitation can be contemplated.

56. It is true that in the United Kingdom the silver currency has a fixed limit of 40*s*., beyond which it cannot be used to pay a debt. But this has not always been the case. Prior to 1774 the English Mint was open to silver, and silver coins were an unlimited tender. In 1774 the tender of silver by tale was restricted to 25*l*. in any one payment, although it was left an unlimited tender by weight. In 1798 the free coinage of silver was stopped altogether, the English Mint being thereby closed to silver. In 1816, when gold monometallism was formally established by law, silver coins were placed on a purely subsidiary footing, with a 40*s*. limit of tender. At the present time the right to coin silver is confined to the Government, who are responsible for seeing that there is no over-issue; and in the exercise of that responsibility no additional silver is coined at the Royal

Mint for the United Kingdom except in response to the automatic demands of trade, as testified by requisitions received through the Banks of England, of Scotland, or of Ireland. Seeing that for every 20*s*. of additional silver coin requisitioned the Banks have to credit the Royal Mint with a sovereign, there is certainly no temptation to them to demand an over-issue, the immediate profit on which would go not to themselves but to Her Majesty's Government. While it cannot be denied that the 40*s*. limitation tends to emphasise and maintain the subsidiary character of our silver coinage, yet the essential factor in maintaining those tokens at their representative nominal value is not the statutory limit on the amount for which they are a legal tender in any one payment, but the limitation of their total issue. Provided the latter restriction is adequate, there is no essential reason why there need be any limit on the amount for which tokens are a tender by law. It is principally to restriction of the total issue of silver coinage in the United Kingdom that we attribute the fact that 20 silver shillings (intrinsically worth at present about 8*s*. 6*d*.) pass current and are freely received, for all purposes of internal currency, indifferently with the sovereign which they purport to represent. By law there is no convertibility of our silver coins into gold. They possess an extra-legal convertibility evinced by their being generally and popularly exchangeable into gold, and this quality they owe essentially to the fact that they are not issued by the Government in excess of the volume required for the purpose which they discharge.

57. Outside the United Kingdom there are two principal instances of countries with a gold standard and currency, which admit silver coins to unlimited tender. These countries are France and the United States of America. In France the five-franc piece is an unlimited tender and for all internal purposes is equivalent to gold. The same remark applies in the United States to the silver dollar. At the present time there is no addition to the coinage either of five-franc pieces or of United States silver dollars. In the case of the five-franc piece there was free coinage up to 1874, in January 1874 the coinage was limited, and in November 1878 it was suspended altogether. With the repeal in 1893 of the purchasing clauses of the Sherman Act, the same result was reached with regard to the United States silver dollar. Both in France and in the United States the mints are now closed to the coinage of silver coins of unlimited tender. In neither country are such coins convertible by law into gold; in both countries alike they are equivalent to gold for all internal purposes. For international payments, so far as specie is concerned, France and the United States depend ultimately on the international medium of exchange, which is gold. In the last resort, it is their gold which, acting through the foreign exchanges, maintains the whole mass of their currency at its nominal value for internal purposes.

58. We do not doubt that it is, in theory, possible to attain the same result in India as in France and the United States

of America by limitation of the quantity of the rupee currency. The special difficulty in the case of India is one of degree and not of principle. We are unwilling to commit ourselves to the acceptance of the estimates which have been made of the number of rupees actually circulating in India. There can be no doubt but that it is very large; and there are also large quantities of rupees in existence which, though not actually circulating, might, under certain conditions, be brought into circulation. On this account, doubts have been entertained in the past whether the mere closing of the Indian mints to silver would, in practice, be attended with such a restriction of the rupee currency as would make the rupee permanently exchangeable for gold at a fixed rate.

The experience which has been gained since the closing of the Indian mints supports the belief that this result will be attained. From the nature of the case, the demand for rupee currency increases every year; there is no evidence that large quantities of rupees that were formerly hoarded have been thrown into circulation since the mints were closed; the exchange has risen steadily since 1894-95, and the rupee is now actually exchangeable for gold at the rate of *1s. 4d.*; while the demand for additional currency has been so great that over *2,370,000l.* in gold has been paid to the Indian Treasury for the purchase of silver rupees.

The forces which affect the gold value of the rupee are complicated and obscure in their mode of operation, and we are unable, therefore, to say positively that the mere closing of the mints to silver will, in practice, lead to such a limitation of the rupee currency, relatively to the demands for it, as will make the rupee permanently exchangeable for gold at a fixed rate; but we have no hesitation in repeating the opinion that the experience of the last few years, so far as it goes, indicates that this result is attainable—if, indeed, it has not already been attained.

59. The position of the currency question in India being such as we have explained in the preceding paragraph, we do not consider it necessary to recommend a different policy in the case of that country from that which is found sufficient in France and the United States, by imposing a legal obligation on the Government of India to give gold for rupees, or, in other words, to substitute the former for the latter on the demand of the holders. This obligation would impose on the Government of India a liability to find gold at a moment's notice to an amount which cannot be defined beforehand, and the liability is one which, in our opinion, ought not to be accepted.

Although the Government of India should not, in our opinion, be bound by law to part with its gold in exchange for rupees, or for merely internal purposes, we regard it as the principal use of a gold reserve that it should be freely available for foreign remittances whenever the exchange falls below specie point; and the Government of India should make its gold available for this purpose, when necessary, under such conditions as the circumstances

of the time may render desirable. For example, the Government of India might, if the exchange showed a tendency to fall below specie point, remit to England a portion of the gold which it may hold,—a corresponding reduction being made in the drawings of the Secretary of State; and, when it has accumulated a sufficient gold reserve, and so long as gold is available in its Treasury, it might discharge its obligations in India in gold, instead of in rupees.

60. The exclusive right to coin fresh rupees must remain vested in the Government of India; and, though the existing stock of rupees may suffice for some time, regulations will ultimately be needed for providing such additions to the silver currency as may prove necessary. The Government should continue to give rupees for gold, but fresh rupees should not be coined until the proportion of gold in the currency is found to exceed the requirements of the public. We also recommend that any profit on the coinage of rupees should not be credited to the revenue or held as a portion of the ordinary balance of the Government of India, but should be kept in gold as a special reserve, entirely apart from the Paper Currency reserve and the ordinary Treasury balances.

VII.

The Sterling Rate for the Rupee.

61. We have now to consider the fixed relation which, under a gold standard for India, the rupee should bear to the sovereign. Hitherto we have dealt in general terms with the question of a gold standard, and our recommendations have pre-supposed a fixed relation, but have not specified the actual rate which should be adopted. We have now to state to your Lordship the conclusions we have reached on this matter.

62. The Government of India proposed in 1892 to close the Indian mints to silver and to pass an Act authorising them to declare gold a legal tender at a rate not exceeding 18*d*. for the rupee. They would not have exercised this power at once, and they would have been guided by circumstances and the experience gained by the closing of the mints in determining what should be the fixed, permanent, legal ratio between the rupee and the sovereign. The rate could not, however, under the law proposed by the Government of India, have exceeded 18*d*. for the rupee, though it might have been lower.

The proposals of the Government of India were generally approved by Lord Herschell's Committee, but the Committee recommended a provisional limit which would prevent the exchange with India from rising materially above 1*s*. 4*d*. for the rupee. The Committee did not recommend that the limit of 1*s*. 4*d*. for the rupee should be the permanent legal ratio between the rupee

and the sovereign. It left the question of the permanent legal ratio between the two coins to be decided in the light of subsequent experience. In paragraph 151 of the Committee's Report the following language is used:—" It would not, of course, be essential to the plan that the ratio should never be fixed above 1*s.* 4*d.*; circumstances might arise, rendering it proper, and even necessary, to raise the ratio; and the Indian Government might be empowered to alter it with the sanction of the Secretary of State. Such a scheme would, indeed, in the first instance, be tentative, and would not impede further action if circumstances should render it desirable."

The modifications of the proposals of the Government of India recommended by Lord Herschell's Committee were accepted, the Indian mints were closed to silver, and a provisional arrangement was made for giving rupees in exchange for gold at the rate of 16*d.* for the rupee.

The maximum limit of 18*d.* for the rupee, originally suggested by the Government of India, was not imposed, and the question of the permanent legal ratio can now be considered in the light of what is expedient in the present day, and unfettered by any promises made, or conditions imposed, in the past.

63. In dealing with this question at the present day, it is desirable to have in view an outline of the whole series of facts of exchange, both before and after the closing of the Indian Mints to silver on 26th June 1893. Starting from the year in which Germany demonetised silver, the following table shows the average rate per rupee at which Council Bills and Telegraphic Transfers on India were sold in London:—

	d.		*d.*
1872-73 . .	22·754	1885-86 . .	18·254
1873-74 . .	22·351	1886-87 . .	17·441
1874-75 . .	22·156	1887-88 . .	16·898
1875-76 . .	21·626	1888-89 . .	16·379
1876-77 . .	20·508	1889-90 . .	16·566
1877-78 . .	20·791	1890-91 . .	18·089
1878-79 . .	19·794	1891-92 . .	16·733
1879-80 . .	19·961	1892-93 . .	14·985
1880-81 . .	19·956	1893-94 . .	14·547
1881-82 . .	19·895	1894-95 . .	13·101
1882-83 . .	19·525	1895-96 . .	13·638
1883-84 . .	19·536	1896-97 . .	14·451
1884-85 . .	19·308	1897-98 . .	15·354
		1898-99 . .	15·978

From these figures it will be observed that, after a fall of about 3*d.* in the first six years, there was comparative stability above 19*d.* for the seven years from 1878-79 to 1884-85; that, apart from the temporary effects of the passing of the Sherman Act in 1890 and the speculation connected therewith, the average rate ranged round 16½*d.* in 1887-88, 1888-89, 1889-90, and again in 1891-92; and that, in 1892-93, the average rate had fallen to under 15*d.* It was under these circumstances that, on 31st May 1893, the

Herschell Committee, in recommending the closing of the Indian Mints to the public, further recommended that rupees should be coined on tender of gold at the Mints "at a ratio to be fixed in the first instance not much above that now prevailing, say **1*s*. 4*d*.** the rupee." They did not propose to go back to the so-called par of 2*s*.; they fixed, provisionally, a maximum limit which was lower by 2*d*. than the limit of 1*s*. 6*d*. proposed by the Government of India. Apart from a momentary rise to 1*s*. $4\frac{1}{32}$*d*. for Telegraphic Transfers on 27th June, the Indian Exchange fell steadily away through the second half of 1893 and through the whole of 1894, until on 23rd January 1895 Council Bills were sold at 1*s*. $0\frac{3}{32}$*d*. From that date onwards there was, on the whole, a steady and a continuous rise of the exchange, and 16*d*. was regained (after an interval of six years) in the early days of January 1898. From the beginning of 1898 up to the present time, a rate of 16*d*. has practically been maintained without a break, the extreme limits of oscillation for Bills being $15\frac{11}{16}$*d*. and $16\frac{1}{8}$*d*.

64. In the year 1898-99 the total volume of the export trade exceeded that of all past years, amounting to over Rx. 120,000,000 and showed a net surplus over total imports of no less than Rx. 30,000,000. As we have pointed out, this result was achieved with a 16*d*. rate of exchange, and without monetary stringency. We have further pointed out that in the year 1898-99 the Government of India has been able to accumulate a gold reserve of 2,378,609*l*., which will contribute towards the maintenance of exchange. Moreover, the continuance of existing arrangements, under which no fresh rupees are coined except in exchange for gold at a fixed rate, must tend more and more to establish the exchange at such rate and to ensure the gradual and automatic introduction of a gold currency to supplement, in response to the growing demands of trade, the relatively shrinking stock of rupees.

65. Although the limit of 1*s*. 4*d*. for the rupee was declared to be merely provisional, it has been regarded generally as the permanent rate at which the Indian monetary standard was to be transferred from a silver to a gold basis. There are some who would prefer a lower rate, and there are others who are prepared to accept a higher rate; but it is not desirable, in the absence of any strong reason, to adopt a rate different from that on which calculations have been based, and which has formed the ground of practical action.

We also desire to point out that the rate of 1*s*. 4*d*. is that of the present day; prices in India may be assumed to have adjusted themselves to it, and the adoption of a materially lower rate at the present time would cause a distinct and, in our opinion, a mischievous disturbance of trade and business. The *onus probandi* rests on those who would now propose a different rate. Between the rate of 1*s*. 4*d*. and the rate determined by the bullion value of the rupee, there is no one rate which can be described as natural or normal, rather than any other rate.

66. Various proposals have been made for disturbing the existing rate by the substitution of another rate. It has been proposed to fix the rate at 1*s.* 1½*d.*, 1*s.* 2*d.*, 1*s.* 2¼ *d.*, 1*s.* 3*d.*, and 1*s.* 6*d.* All these proposals are arbitrary, and involve a dislocation of the existing ratio between rupee prices and sterling prices. For such disturbance no adequate reasons, in our opinion, have been adduced. In great part these proposals (other than that of 1*s.* 6*d.*) are based on the belief that a lower sterling value of the rupee would cause a rise in rupee prices, benefit the Indian producer, check consumption of foreign goods, and so affect the balance of trade as to promote the importation of gold needed for expanding the volume of currency to an extent commensurate with the rise in the scale of prices.

In our opinion a rise in prices which expresses only the depreciation of the currency is no gain to the community as a whole, and, although the fixing of a lower denomination in sterling for the rupee might for a time give some advantage to producers and induce for a limited period a larger importation of gold than would otherwise take place, this would be at the expense of every holder of a rupee, or debt or security for a fixed amount of rupees; and the taxpayer would again be compelled to provide a larger amount of currency to meet the sterling requirements of the State. It is not by such an expedient as the writing-down of the rupee in sterling that a permanent stimulus can be given to production or to the importation of the standard metal. We see no sufficient reason for altering the existing relations of prices and the essential conditions of contracts expressed in Indian currency, or for reversing the course of exchange and returning to some basis of value which may have prevailed during the interval between the fall and partial recovery in the sterling value of the rupee, and which does not possess elements of permanent stability in a higher degree than the present rate. We are, therefore, of opinion that the permanent rate should be that which has been adopted as the provisional rate in the past, and which is also the market rate of to-day, *viz.*, 1*s.* 4*d.* for the rupee.

67. In recommending a fixed legal rate of 1*s.* 4*d.*, we are not unanimous, though the majority hold the views we have just expressed.

One of our number would not fix the permanent rate at once, but would leave that question to be decided in the light of further experience,—the final rate being fixed either below or above 16*d.*, as further experience might show to be expedient. We are of opinion that any advantage which might arise from this course is more than counterbalanced by the importance of removing doubts as to the future policy of the Government of India, and giving increased confidence to those who are engaged in commercial and financial business in connection with the Indian Empire.

68. Two other Members of the Committee are not prepared to accept the rate of 1*s.* 4*d.*, and recommend that it should be fixed at 1*s.* 3*d.*

It is argued that the rate of 1*s*. 3*d*. will be more favourable to the Indian export trade than 1*s*. 4*d*.; but we have already expressed the opinion that any advantage to the export trade that is gained in this way, is gained at the expense of other members of the community, and is only temporary. If the rate is to be fixed at 1*s*. 3*d*. in order to benefit the Indian exporters and the Indian producer of articles of export, the same argument would justify a further reduction to 1*s*. 2*d*., and so on, without any limit which we have been able to discover. Nor do we think there are any good grounds for holding that the gold standard cannot be established in India at 1*s*. 4*d*., while it can be established at 1*s*. 3*d*.

If it is impossible at 1*s*. 4*d*., it will be impossible at 1*s*. 3*d*.; and we have already dealt in paragraph 66 with the question of the temporary loss and gain to individuals and classes of the community caused by a lowering of the existing rate of exchange. We would add that, if the exchange were now lowered from 1*s*. 4*d*. to 1*s*. 3*d*., the classes of the community who would gain are those who have already gained through the fall from 2*s*. to 1*s*. 4*d*., and the classes who would lose are those who have already lost through that fall. Stronger reasons than appear to us to exist would be needed to justify a measure which would have the effect of adding to the gains of the former classes and intensifying the losses of the latter.

It is said that the conditions prevailing in 1893 show that 1*s*. 3*d*. is the rate that should have been adopted at that time. We do not accept this argument, and the conditions have changed since 1893. The rate of 1*s*. 3*d*. may have prevailed shortly before the mints were closed, but the rate of that time was a fluctuating rate. If the mints had been closed some years earlier, and the market rate had been adopted, the permanent rate would have been considerably higher than 1*s*. 4*d*.; if they had been closed some years later and the same principle had been followed, the permanent rate would have been lower than 1*s*. 3*d*. As we have already said, between the rate of to-day and that determined by the bullion value of the rupee, there is none which can be described as natural or normal; and we can find no good reason for making the permanent rate depend upon the accident of the date on which the Indian mints were closed to silver.

It is true that Lord Herschell's Committee remarked that " to close the mints for the purpose of raising the value of the rupee is open to much more serious objection than to do so for the purpose of preventing a further fall;" but an undue stress is laid on these words when they are used as an argument against permanently adopting a rate of 1*s*. 4*d*., since that Committee actually adopted a provisional rate of 1*s*. 4*d*. and expressly said that circumstances might arise rendering it proper, and even necessary, to raise the rate.

69. We recommend that there should be no change in the existing relation of the rupee to the sovereign. The experience

gained since the mints were closed in 1893, and particularly that of the last eighteen months, appears to us to justify the anticipation that the existing rate of 1*s.* 4*d.* will, with possible temporary fluctuations, due to the course of trade, be maintained in the future.

VIII.

70. In conclusion, we desire to record our opinion that* the effective establishment of a gold standard is of paramount importance to the material interests of India. Not only will stability of exchange with the great commercial countries of the world tend to promote her existing trade, but also there is every reason to anticipate that, with the growth of confidence in a stable exchange, capital will be encouraged to flow freely into India for the further development of her great natural resources. For the speedy attainment of this object, it is eminently desirable that the Government of India, with whom it will rest to decide when successive steps should be taken, should husband the resources at their command, exercise a resolute economy, and restrict the growth of their gold obligations.

71. We desire to express our high appreciation of the assistance which Mr. Chalmers has rendered to us throughout the whole course of this inquiry. We feel it to be our duty to recognise in the strongest terms the knowledge, ability, courtesy, and industry which he has displayed and which have greatly facilitated our labours.

HENRY H. FOWLER.
BALFOUR OF BURLEIGH.
*JOHN MUIR.
FRANCIS MOWATT.
D. BARBOUR.
C. H. T. CROSTHWAITE.
ALFRED DENT.
F. C. LE MARCHANT.
E. A. HAMBRO.
W. H. HOLLAND.
*ROBT. CAMPBELL.

ROBERT CHALMERS,
Secretary.

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* Subject to a reservation as to the ratio to be adopted between gold and the rupee and the points connected with that question in regard to which our views are expressed in the subjoined Note.

Although I am aware that the question of the banking facilities of India was not referred to the Committee, I venture to call special attention to the first part of paragraph 22 where it is pointed out that they have not of late years kept pace with the increasing trade, and further, to draw attention to the fact that it has been considered wise in Europe to entrust the carrying out of currency laws to banks established or strengthened for that purpose. In my opinion, a strong bank, properly constituted, would be a powerful assistant in giving effect to any regulation having the convertibility of the rupee in view, and that, working under proper currency regulations, such a bank would be likely to carry them out in a more effective way, and in a manner more in harmony with the trade wants of the country, than any Government Department, however well administered, could possibly do.

I venture to call attention to this point because I believe that the success of the recommendations of the Committee, if adopted, will very much depend on the banking wants of the country being assisted in times of pressure, and curtailed in times of slackness; and this, in my opinion, could only be done by the establishment of some institution having ample facilities at its disposal, and framed on somewhat similar lines to those of either the Bank of England or the Bank of France.

E. A. HAMBRO.

Since the Committee was appointed, the condition of the money market in India has so greatly improved that the immediate settlement of the currency question has, in my opinion, become less urgent than it was in the spring of 1898.

Under existing conditions, gold is not—in form—a legal tender in India; yet, for all practical purposes, the sovereign is now a legal tender for 15 rupees, because the holder of a sovereign can obtain for it 15 rupees at the Government Treasury, and these 15 rupees constitute a legal tender. To make the sovereign a legal tender at the rate of 15 rupees, is therefore only a change in form and not in substance, and will neither strengthen exchange, nor be likely to lead to a greater import of gold into India.

It may be that further experience will show the balance of advantage to lie with a lower exchange than 1*s*. 4*d*.; or, on the contrary, circumstances might conceivably arise (*e.g.*, silver legislation in the United States) which would necessitate a higher rate. In view of these possibilities, and of the fact that the existing monetary conditions of India are not, in my judgment, producing any serious evils, I am of opinion that no action should be taken at the present time, in the direction of finally settling the rate between the sovereign and the rupee; but that the question should be left to be decided in the fuller light which would be afforded by further experience.

Subject to these remarks, I am in general accord with the principles of the Report.

W. H. HOLLAND.

We do not admit that the experience of the last six years justifies the adoption of a 1*s*. 4*d*. ratio. For five years after the closing of the mints exchange never effectively reached that level in the sense of bringing gold to the currency; and, while giving due weight to the fact that during the last six months the Currency Department has received a considerable amount of gold, we cannot agree that a single year of unprecedentedly large exports, arising from exceptional causes, is a sufficient basis for assuming that this will continue to the extent necessary for India's currency requirements. The great rise in the price of wheat in April/June of last year increased the Indian exports of that article to Rx. 9,720,333, as compared with Rx. 1,341,151 in 1897-98 and an average of Rx. 2,750,137 in the five years 1893-94 to 1897-98 inclusive. The exports of rice were also Rx. 3,500,000 above the average of the previous five years. But for these exceptional causes, last year's total exports would not have been unusually large, and it may be questioned whether gold would have found its way to India as currency in any quantity.

A review of the circumstances which accompanied the closing of the mints, is sufficient to show that the violent disturbances which unsettled exchange for several years, were mainly due to the arbitrary enhancement of the rupee to 1*s*. 4*d*. On 31st May 1893, the date of the Herschell Committee's Report, exchange stood at 1*s*. 2⅝*d*. It will be remembered that although the Report was not made public till the 26th June, the day the mints were closed, its purport became known to a group of speculators almost as soon as it was signed (a correct summary was published in a continental newspaper on the 7th June). This led to immense speculation in exchange and rupee paper, in connection with which unusually large remittances were made to India. Between the 31st May and the 6th June no less than Rx. 3,780,000 Council bills were taken, and in addition 1,180,000*l*. of bar silver was shipped. It was then believed that the closing of the mints would establish a 1*s*. 4*d*. rate, and consequently there was a strong movement to remit money out at anything under it. Exchange touched 1*s*. 4*d*. for a day on the 27th June, but it soon became apparent that the rise had been overdone, and the downward movement which followed, assisted by the plethora of money arising from the above operations, carried exchange as much below its level as it had previously been forced above it. Had a 1*s*. 3*d*. rate been adopted, these wide fluctuations would not have taken place; and we believe the market would have settled down to it without much difficulty, that gold would have gone to India as currency to a fair extent in 1896-97 if not earlier, and to a larger extent in 1897-98, and that the intense monetary stringency of these two seasons would have been avoided.

When exchange began to advance after touching its lowest point on the 23rd January 1895, it gradually recovered without any pressure on the money market till 1*s*. 3*d*. was reached in November 1896. The Presidency Banks' rates were then 6 to

8 per cent., the latter being the highest rate touched during the period in question. It was only when exchange began to rise above 1*s*. 3*d*. that stringency was experienced; and that the raising of the rate by the additional penny required to bring relief in the shape of gold, became a difficult process accompanied by extreme monetary pressure.

These considerations appear to us to point to 1*s*. 3*d*. as the ratio which should be adopted rather than a forced ratio of 1*s*. 4*d*.

The advocates of a 1*s*. 4*d*. ratio point to the fact that this rate has now been, more or less, effective for the last 18 months, thereby establishing a *status quo* which it would be unwise to disturb. This argument would have greater weight if the *status quo* had been arrived at in a natural way; but the circumstances under which it was reached have only to be considered to deprive it of any value. With no fresh currency otherwise obtainable, the monopoly rupee was bound in time to rise to whatever gold point the Indian Government chose to fix, and the fact of its having risen in five years to 1*s*. 4*d*. is of itself no more a proof that 1*s*. 4*d*. is an equitable ratio than it would be in regard to 1*s*. 6*d*. or 1*s*. 8*d*., which could equally be reached in course of time. To arrive at a rate in this manner and then point to the accomplished fact as disposing of any question of its propriety is not convincing, especially if there is reason to believe that a rupee so greatly enhanced is calculated to have an injurious effect on the country's interests and to retard or even jeopardise the success of the gold standard.

We approve of the principle that India should be allowed to acquire the necessary gold by means of the trade balance in her favour. But to enable her to do so, anything calculated to injure that balance should be avoided. This is equally imperative on the ground that it is on the trade balance that India also depends for the power to meet her foreign obligations; and the rate of exchange, or the ratio fixed between gold and the rupee, is of the greatest importance in its bearing on her ability to maintain a balance of exports over imports, sufficient to meet both these requirements.

The Committee have obtained a great deal of evidence as to the effect of exchange on trade, and, although opinions differ, this at least is undoubted, that the rate of exchange has a direct influence on the rupee prices of articles of export and import. A lower exchange gives the Indian exporter a higher rupee price for his produce, without raising the gold price to the foreign buyer, while compelling an importer of foreign goods to exact a higher rupee price to cover his gold outlay. A higher exchange on the other hand lowers the rupee price of native produce, while enabling the foreign importer to sell his goods cheaper. An appreciated exchange through its action on prices has thus a double effect on the trade balance, by checking exports and stimulating imports. And that this is not of the temporary character

which some maintain is shown in India's opium trade with China.

Owing to the closing of the mints, China exchange on India has fallen from about 306 rupees per 100 taels in 1892-3 to the present level of about 204 rupees, it has been even lower; thus necessitating a higher price for opium in China to give the Indian exporter the same rupee return. Viewed in this light, the course of the trade is instructive.

There has been an advance in the tael price in Shanghai from an average (Patna, Benares, and Malwa together) of about 397 taels per picul in 1892 to 556 taels in 1897, notwithstanding which the price in India has fallen from an average of about Rs. 1,202 per chest in the former year to about Rs. 1,114 in the latter, while Indian exports have diminished from 75,384 chests in 1892-3 to 56,069 chests in 1897-98.* We thus see the effect of the enhanced rupee in a falling off in the Indian exports and a lower rupee price,—the rise in the tael price, large as it is, not having gone far enough (being checked by the stimulus given to Chinese native competition) to enable India to export to the same advantage in face of the adverse exchange. Looked at from China's point of view, the effect of the fall in the tael exchange in checking imports into China is equally apparent, and the truth of the principle that a rise in exchange checks exports and stimulates imports, while a fall has the contrary effect, is thus shown in the trade of both countries. In the Budget Statement of March 1899, paragraph 166, the Finance Minister makes the following comment in his remarks on opium:—"The growing competition of the China drug has prevented the price in China from rising in proportion to the increased value of the rupee due to the currency legislation of 1893." For "increased value of the rupee" read "fall in the China exchange on India," and there could not be a clearer confirmation of the effect of the enhancement of the rupee on India's opium trade. It must be added that the export of opium to China increased last year to 67,128 chests, which is explained in the same paragraph to be "largely due to a scanty crop in China."

The opium trade has been described as a dwindling trade at the best, but it is impossible to doubt that the falling off in the last six years is largely due to the enhanced rupee.

Another branch of India's trade with the Far East—her exports of cotton, cotton yarn, and goods—is also exposed to a danger which it would be unwise to aggravate by pushing the enhancement of the rupee too far. Within the last few years an important cotton mill industry has sprung up in China and Japan for the supply of their home markets, although the effect on India has scarcely yet had time to manifest itself for two reasons,—first, that Japan uses Indian cotton largely in her mills, which, so far,

* These figures are taken from the "Financial and Commercial Statistics," up to the end of 1897, published by the Government of India. The volume embracing 1898 is not yet issued.

places her products on a level with those of India,* and, secondly, because the China mills only came into operation in the end of 1896 (Q. 12, 493), so that the industry is still in its infancy. The conditions, however, which have assisted the competition of China-grown against Indian opium may in time be equally effective in regard to cotton. There are indications that the cultivation of cotton is extending (Consular Report, p. 57, Vol. II), and, if Japan should find it more advantageous to buy her cotton in China, a serious blow may in time be dealt to another branch of India's export trade.

We do not ignore the evidence as to the appreciation of copper cash, which as the usual wage-paying medium in China must largely govern the cost of production. We are told (Q. 8,250-2) that it has appreciated in relation to silver about 15 per cent. in the last five or six years. This represents less than half the fall in the China exchange, so that a modification of the present enhancement of the rupee is still necessary to put India on fair terms of competition with China.

India's disadvantage is not less real in her competition with silver standard countries for the export trade to neutral markets. As regards tea, China with her dollar at its bullion value will be greatly assisted by an enhanced rupee in her endeavours to recover her former predominant position. Although her exports of tea to the United Kingdom are now comparatively small, her total exports amounted to 205,000,000 lbs. last year. Her productive power is, therefore, by no means crippled, and it would be a mistake to think that India can afford to disregard her competition.

In principle, the effect of an enhanced rupee equally applies to India's trade with gold standard countries, although as sterling exchange has never fallen to the silver bullion point it may be less marked.

Without going so low as that point or even the lowest rate touched since 1893, the arbitrary enhancement of the rupee has been considerable, and the step taken that year went a good deal beyond merely checking a further fall. Referring to the Report of the Herschell Committee, we find that, after discussing at some length the probable effect on Indian trade of a rupee divorced from its bullion value, they made the following important statement in paragraph 135:—"It is impossible, in view of these considerations, not to come to the conclusion that to close the mints for the purpose of raising the value of the rupee is open to much more serious objections than to do so for the purpose of preventing a further fall." The value of the rupee on the 31st May 1893, the date of the Committee's Report, was 1*s*. 2⅝*d*., and it is difficult to reconcile the above declaration with their conclusion recommending a ratio of 1*s*. 4*d*., or more than 9 per cent. higher. Even applying the expression "preventing a further

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* Although Japan is on a gold basis, it is at a ratio equivalent to 11¼*d*. per rupee as compared with India's 1*s*. 4*d*.

fall" to the date of their appointment, the 21st October 1892, the rate of exchange then was 1*s.* 3·06*d.*, on which 1*s.* 4*d.* represents an enhancement of 6 per cent.

As to the compensating adjustments which are said to make up to the producer for the smaller rupee price he has to accept for his produce in consequence of a higher exchange, we are unable to see where they are to come from—they have not yet been arrived at in the case of opium. The evidence shows (Q. 9612-6) that wages in India, that is cost of production, have not fallen since the rupee was at 12½*d.* four-and-a-half years ago, nor does it appear that any fall is likely, even if such a thing were desirable, so that there is no compensation to be looked for in that direction, nor do we think it can be expected from a rise in the sterling prices of those articles in which India competes with other countries. Indian wheat, for instance, has to compete in the European markets with the wheat of Europe, the United States, Canada, Argentina, etc., and forming but a small proportion of the total supply can have an equally small influence in determining movements in the price. If a rise in the sterling exchange renders it necessary that India should get a higher price for wheat in England to give her the same rupee return, is it likely that the holding back for a higher price of a few thousand tons of Indian wheat will have any appreciable effect in that direction while the home supplies and the imports from these other countries are pouring in as usual? Any attempt to establish a rise for India's benefit would at once be swamped by increased supplies from other quarters. The market will not concern itself with the larger or smaller rupee outturn realised by the Indian grower, who will either have to take the current price or do without; and the lower rupee price caused by the higher exchange must therefore represent a loss to the producer.

It is on this aspect of the question that we base our strongest objection to the 1*s.* 4*d.* ratio,—its effect as an unfair tax on native production while conferring a bounty on imported goods. It is not a sufficient reply to this to say that, as imports are paid for by exports, the gain and loss to the community are equal. This is evident when we consider that the native producer is the class which loses while the class which gains is the consumer of imported goods. It can never be sound policy to handicap native industry while giving a bounty to foreign imports, and in the case of India with large foreign obligations, which can only be met by surplus exports of produce, it would be a fatal course to pursue. But beyond the effect on exports and imports so far as they balance each other, it still remains that with a 1*s.* 4*d.* exchange the cost of providing at Rs. 15 each the 17 million sovereigns annually required for the home charges is a tax which falls entirely on the producer. The more the rupee is enhanced—the lower the sovereign is valued in rupees—the more cheaply can the Government make its annual remittances. But this advantage is not obtained without being paid for, and the question who

pays is not difficult to answer;—it is the producer, who has to accept so many fewer rupees for the produce he has to sell. If with a 1*s*. 4*d*. exchange the holder of a sovereign can only get Rs. 15 for it, he cannot afford to pay so many rupees for a ton of Indian produce as if with exchange at 1*s*. 3*d*. he could convert his sovereign into Rs. 16. To deny that arbitrary enhancement of the currency is a tax, and to argue that the producer is no worse off in the long run, that wages and other charges must in time adjust themselves to its altered value, is to maintain the dangerous principle that the Government may lighten its liabilities without injury to anybody by a step of this kind. Such a step is undoubtedly a tax on production, and if the Government plead that in the absence of any other available source of revenue trade must bear it, it is unwise to throw the whole of it on one side of trade, the side which it is least expedient to tax, and to penalise production while giving a bounty to foreign imports. The present duty on imports does not counterbalance the bounty conferred by a 1*s*. 4*d*. exchange, and the burden would be more equitably adjusted by reducing the ratio to 1*s*. 3*d*. In addition to its beneficial effect on trade this would relieve production by about 6¼ per cent., while depriving foreign competition of a corresponding bounty, and last year's favourable Budget gives ground for the hope that the additional cost to the Government would be made good out of existing sources of revenue.

The ratio is still an open question. In his speech introducing the Act of 1893, Sir David Barbour stated that it was left open to be decided by the light of future experience. The Government, therefore, are not committed to 1*s*. 4*d*., they are perfectly free to alter the ratio now without exposing themselves to any charge of weakness or breach of faith. The desirability of adhering to existing conditions should not be allowed to weigh at the present stage. Whatever objections there may be to altering the ratio now, they are trifling in comparison with what will be experienced later, should the present ratio not be found practicable. To amend the ratio now would only be to act on the reservation made in 1893, to do so later, after having formally adopted 1*s*. 4*d*. would be a much more serious matter.

The test of a proper ratio is not merely that it should enable the Council Bills to be absorbed, or even its power to attract gold in an exceptionally prosperous year. It should be such as to do so in normal times sufficiently to provide for any drain occasioned by an exceptional adverse season, and to allow gold to gradually accumulate and supplement silver in the currency. To aim at a ratio which would fail to accomplish this for the sake of getting a high price for the Council Bills, would be to starve the currency, injure trade, and invite an ultimate breakdown. As India is debarred from obtaining any fresh silver currency, no difficulty should be placed in the way of her requirements being satisfied by gold. The ratio adopted should, therefore, be one which will encourage the free inflow of gold rather

than one which, even if it might attract some gold in a year of unusually large exports, would fail to do so in ordinary times. In the one case Indian trade would have the advantage of a full supply of currency and easy rates of interest; in the other it would be continually harassed by monetary stringency and by a lame and inefficient currency system which would, sooner or later, prove a failure.

The success or otherwise of the gold standard will largely depend on the rupee value put upon the sovereign. The higher the rupee is raised above its bullion value, the more difficult will the establishment of the gold standard become. On the value put upon the sovereign will depend not only the extent to which gold is brought into the currency, but also how far it will be allowed to remain in circulation, or will disappear, driven out by the over-valued rupee. It is significant that, of the immense amount of gold held in India, practically none has been tendered to the Currency Department, even during periods of extreme monetary pressure. What has been acquired has, with a trifling exception, been imported gold.* This is not reassuring as to the result when gold is made legal tender and a sovereign and Rs. 15 are supposed to be mutually interchangeable. India is a large consumer of gold, and to undervalue it in relation to the rupee will have the effect, not only of discouraging its tender to the Mint, but of encouraging the market to supply itself by withdrawals from the currency. The successful establishment of a gold standard will not be promoted by insisting on getting gold too cheap.

Going back to 1893, the conditions then prevailing clearly pointed to 1*s*. 3*d*. as the ratio which should have been adopted then; and we can see nothing in subsequent experience to justify the belief that 1*s*. 4*d*. is the more suitable ratio now. On the contrary, we consider 1*s*. 4*d*. an extreme ratio, which imposes too severe a tax on production, and is calculated to injure the trade balance necessary for India's solvency, and that the corresponding ratio, of Rs. 15 per sovereign, by putting too low a value on gold, will tend to prevent its going into or remaining in circulation, and thereby endanger the success of the gold standard.

We believe 1*s*. 3*d*., or Rs. 16 per sovereign, to be a ratio which would not be injurious to India's interests, and under which she would be able to acquire by trade influences the gold necessary to make the gold standard effective. We therefore recommend that the ratio should be altered from 1*s*. 4*d*. to 1*s*. 3*d*., or to Rs. 16 per sovereign, instead of Rs. 15.

In making this recommendation, we cannot be regarded as advocating a depreciated currency, in the true sense of the phrase. We are a long way from the point at which the term depreciation would be appropriate;—the rupee at 1*s*. 4*d*. is, on the con-

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* Of Rx. 3,430,000 received by the Currency Department upto 19th June last, only Rx. 42,500 in Bombay and a trifling amount in Calcutta came from gold held in India; the balance was all imported.

trary, immensely appreciated, and in urging a change to 1*s*. 3*d*. we are only seeking to correct what we consider to be an excessive, arbitrary enhancement.

ROBT. CAMPBELL.
JOHN MUIR.

Sterling borrowing in order to acquire gold is so prominent a feature of the Government of India's proposals and of other schemes which have been put before the Committee, that we consider it desirable that the principle of borrowing for such a purpose should be thoroughly examined.

Sterling borrowing is in itself objectionable on the ground that it aggravates the exchange difficulty by permanently increasing the home charges, but there are special reasons besides against borrowing for the purpose of establishing and maintaining a gold standard. If India is unable to acquire gold except by borrowing, that alone would go far to prove her unfitness for a gold standard and her inability to retain gold so acquired. Gold attracted to the currency by trade influences might reasonably be expected to remain in circulation, but there could be no certainty that gold brought in by borrowing would do so; the presumption would be rather the other way, because, short of withdrawing rupees to make room for it (a proposal which has been universally condemned), it is difficult to see how borrowed gold could be introduced into the circulation without creating monetary conditions which would drive it back to England again.

If, however, as we believe, India is able to obtain the necessary gold by means of the trade balance in her favour in the same way as she formerly obtained her silver currency, why should the expensive and objectionable method of borrowing be resorted to? The only advantage of borrowing would be to hasten convertibility, an advantage which would be gained at the expense of any assurance of ultimate success, or any certainty that the borrowed gold would not begin to disappear as soon as convertibility was attempted, while the disturbing influence on the Indian money markets of bringing in large amounts of borrowed gold would not be wholesome. A measure on the other hand under which gold would flow to India gradually as trade and currency requirements dictated, even if it took several years to introduce into the circulation sufficient to make the standard fully effective, would carry with it a confidence which could never be inspired by the sight of gold forced in by artificial means, while the automatic supply of currency as from time to time required would keep the money markets from either undue plethora or stringency.

Italy furnishes a practical illustration of the result of attempting to establish a gold standard by means of borrowed gold. The Italian Government obtained by sterling loans a large amount of gold for that purpose, but they have not succeeded in their

endeavour. They dare not allow the gold they borrowed to go into circulation, because it would at once be exported. At the present rate of Italian exchange the gold, if obtainable, would give a profit of 6 to 7 per cent. to send abroad, and, with the foreign exchange so much above the gold point, the gold standard has disappeared.

A further objection to forcing gold into the currency by borrowing, is the effect it would have in obscuring the proper ratio between gold and the rupee, the ratio at which a gold currency would be practicable, and the mischievous effect it might have in enforcing for the time a ratio which without the continued support of borrowed gold might prove to be unworkable and would therefore ultimately break down. With 120 crores of rupees in circulation, which must continue to be unlimited legal tender for years to come, the change from a silver to a gold-standard is not the simple question of raising so much gold and putting it into circulation at any arbitrary ratio to the rupee which may be chosen. The lower gold is valued in relation to the rupee, the greater will be the difficulty of keeping it in circulation and the greater the danger of the under-valued gold disappearing, leaving the sterling debt as the only lasting result of the operation. A gold standard and currency can only be established and maintained on conditions which will permit of gold flowing freely to India in obedience to trade requirements, and any measure which attempts to override these conditions and force gold in by artificial means will break down sooner or later.

For these reasons we are opposed to sterling borrowing, whether for the establishment or the maintenance of a gold standard. Borrowing to support the standard once resorted to, it would be impossible to know when to stop, and the only safe course is not to begin. It is on trade support that the maintenance of the gold standard must in the long run depend, and any saving of delay through borrowing would not be worth the risk of finding, after having incurred a load of sterling debt with its consequent addition to the home charges, that an impracticable scheme had been pursued which when left to its own merits would break down.

ROBT. CAMPBELL.
W. H. HOLLAND.
JOHN MUIR.

THE ROYAL COMMISSION.

GEORGE, R. I.

George the Fifth, by the Grace of God, of the United Kingdom of Great Britain and Ireland and of the British Dominions beyond the Seas, King, Defender of the Faith, Emperor of India, to

Our Right Trusty and Well-beloved Counsellor Joseph Austen Chamberlain;

Our Right Trusty and Well-beloved Edmund Beckett, Baron Faber;

Our Right Trusty and Well-beloved Arthur, Baron Kilbracken, Knight Grand Cross of Our Most Honourable Order of the Bath; and

Our Trusty and Well-beloved:—

Sir Robert Chalmers, Knight Commander of Our Most Honourable Order of the Bath, Permanent Secretary to the Treasury;

Sir Ernest Cable, Knight, formerly President of the Bengal Chamber of Commerce;

Sir Shapurji Burjorji Broacha, Knight, formerly Sheriff of Bombay;

Sir James Begbie, Knight, Secretary and Treasurer of the Bank of Bombay;

Robert Woodburn Gillan, Esquire, Companion of Our Most Exalted Order of the Star of India, Secretary to the Government of India in the Finance Department;

Henry Neville Gladstone, Esquire; and

John Maynard Keynes, Esquire, Fellow of King's College in Our University of Cambridge, and Lecturer in Economics,

Greeting!

Whereas We have deemed it expedient that a Commission should forthwith issue

To inquire into the location and management of the general balances of the Government of India; the sale in London of Council Bills and Transfers; the measures taken by the Indian Government and the Secretary of State for India in Council to maintain the exchange value of the rupee in pursuance of or supplementary to the recommendations of the Indian Currency Committee of 1898, more particularly with regard to the location, disposition, and employment of the Gold Standard and Paper Currency Reserves; and whether the existing practice in these matters is conducive to the

interests of India; also to report as to the suitability of the financial organisation and procedure of the India Office; and to make recommendations:

Now know ye, that We, reposing great trust and confidence in your knowledge and ability, have authorised and appointed, and do by these Presents authorise and appoint you, the said Joseph Austen Chamberlain (Chairman); Edmund Beckett, Baron Faber; Arthur, Baron Kilbracken; Sir Robert Chalmers; Sir Ernest Cable; Sir Shapurji Burjorji Broacha; Sir James Begbie; Robert Woodburn Gillan; Henry Neville Gladstone and John Maynard Keynes to be Our Commissioners for the purposes of the said enquiry.

And for the better effecting the purposes of this Our Commission, We do by these Presents give and grant unto you, or any three or more of you, full power, at any place in Our said United Kingdom of Great Britain and Ireland, to call before you such persons as you shall judge likely to afford you any information upon the subject of this Our Commission; and also to call for, have access to and examine all such books, documents, registers and records as may afford you the fullest information on the subject, and to inquire of and concerning the premises by all other lawful ways and means whatsoever.

And We do by these Presents authorise and empower you, or any three or more of you, to visit and personally inspect such places as you may deem it expedient so to inspect for the more effectual carrying out of the purposes aforesaid.

And We do by these Presents will and ordain that this Our Commission shall continue in full force and virtue, and that you, Our said Commissioners, or any three or more of you, may from time to time proceed in the execution thereof and of every matter and thing therein contained, although the same be not continued from time to time by adjournment.

And We do further ordain that you, or any three or more of you, have liberty to report your proceedings under this Our Commission from time to time, if you shall judge it expedient so to do.

And Our further will and pleasure is that you, with as little delay as possible, report to Us under your hands and seals, or under the hands and seals of any three or more of you, your opinion upon the matters herein submitted for your consideration.

Given at Our Court of St. James's, the seventeenth day of April, one thousand nine hundred and thirteen, in the third year of Our Reign.

By His Majesty's Command,

R. McKENNA.

Indian Currency and Finance.
Royal Commission of Inquiry.

CONTENTS.

Royal Commission on Indian Finance and Currency, 1914.

REPORT TO THE KING'S MOST EXCELLENT MAJESTY.

MAY IT PLEASE YOUR MAJESTY,

WE, the undersigned Commissioners appointed to inquire into the location and management of the general balances of the Government of India; the sale in London of Council bills and transfers; the measures taken by the Indian Government and the Secretary of State for India in Council to maintain the exchange value of the rupee in pursuance of or supplementary to the recommendations of the Indian Currency Committee of 1898, more particularly with regard to the location, disposition, and employment of the Gold Standard and Paper Currency Reserves; and whether the existing practice in these matters is conducive to the interests of India; also to report as to the suitability of the financial organisation and procedure of the India Office; and to make recommendations; humbly submit to Your Majesty the following Report:—

I.—INTRODUCTORY.

1. We have held 34 meetings and have examined 33 witnesses. In order that full opportunity might be given for an expression of the views of the various persons and bodies interested in the subjects of our inquiry, we decided at our first meeting to request the Government of India through the Secretary of State to issue a public invitation in India for representative witnesses to appear before us; and arrangements were made for facilitating the attendance of those who had to travel specially from India to London for this purpose. Twelve witnesses representative of the commercial, financial, and banking interests throughout India attended as the result of this invitation; while two other witnesses, Mr. Marshall Reid, C.I.E., and Mr. M. de P. Webb, C.I.E., who attended in response to our direct invitation, may be included in the same category. Several others, who were prevented from one cause or another from fulfilling their original intention of appearing before us for examination, have submitted statements of their views, which are printed among the appendices to our Reports, together with similar statements from others who were either unable to accept the invitation to give oral evidence or were asked by us to express their views in writing instead of attending in person.

2. Of the remaining nineteen witnesses, two were former chairmen of the Finance Committee of the India Council; one is the

present chairman and one a present member of that Committee, one is the broker to the Secretary of State for India, and four are members of the India Office permanent staff, making nine witnesses in all who were directly or indirectly representatives of the India Office. The Government of India selected four witnesses to represent them, including Mr. Bhupendra Nath Mitra, C.I.E., Assistant Secretary to the Government of India in the Finance Department, and Sir James Meston, K.C.S.I., now Lieutenant-Governor of the United Provinces, and a former Secretary in the Finance Department. In addition to these official representatives of the Government of India, Sir Guy Fleetwood Wilson, K.C.S.I., etc., who had recently retired from the position of Finance Member of the Viceroy's Council, and Mr. F. C. Harrison, C.S.I., a former Accountant-General at Bombay, attended as witnesses at our invitation.

3. The remaining four witnesses comprise a representative of the Bank of England, two representatives of the Exchange Banks doing business in India, and Mr. Moreton Frewen, who came before us at his own request. His special object was to express the views of those who desire to see the Indian mints re-opened to the unrestricted coinage of silver.

4. Our reference indicates the following main subjects for our inquiry: the general balances of the Government of India and of the India Office in India and London respectively: the sale of Council drafts by the Secretary of State in London: the Gold Standard Reserve: the Paper Currency Reserve: the system by which the exchange value of the rupee is maintained: and the Financial Organisation and Procedure of the India Office.

5. At a very early stage in our inquiry we came to the conclusion that we could not deal adequately with these subjects unless we also considered the questions of the establishment of a Central or State Bank for India, and the provision of facilities in India for the coinage of gold.

6. All these questions are closely interconnected. Much of the criticism directed against the Indian Government and the India Office, both in the evidence given before this Commission and elsewhere, has been founded on a mistaken attempt to deal with one or other of these questions separately, and a failure to consider the Indian financial and currency system as a whole. This tendency has been accentuated by the absence of any full or clear exposition of that system by the responsible authorities. The appendices to our reports contain a series of official memoranda and despatches which go far towards filling this gap, whilst the historical summary which we give in the next section should suffice to make that system, its objects and its methods, readily intelligible to anyone who is interested in them.

7. This system is the outcome of the reports of two Committees anterior to this Commission as modified or developed by the experience gained in succeeding years. It must be remembered that even the Committee of 1898 had little experience to guide them. Some of

their recommendations were tentative and experimental. They contemplated developments, the exact course of which it was impossible for them to foresee, and they certainly had no desire to bind the Government of India to a particular solution of questions of detail which further experience might show to be unnecessary or undesirable. Their main object was to establish a stable rate of exchange, and all their other recommendations were directed to this great purpose. It is no matter for surprise if, in applying a novel policy to constantly changing conditions, official declarations have not always been entirely consistent or official action always free from hesitation. But we desire at the outset of our report to record our high opinion of the ability and skill with which the complicated duties connected with Indian finance have been discharged by the permanent officials to whom they have been entrusted both in India and in London. Lord Inchcape, who had special opportunities of judging of their work and whose wide experience of business gives special weight to his judgment, summed up his opinion in the words (*qu.* 10,867), "I have often wished that I had some of them in my office," whilst Sir Felix Schuster, the present chairman of the Finance Committee, spoke (*qu.* 10,987) of "the great ability and businesslike manner with which the work was carried on by the officials." Those of us who have had no official connection with Indian administration or the India Office express our hearty concurrence in this well merited praise.

8. Much of the report of the Committee of 1898 was occupied with the discussion of the merits of the policy of closing the Indian mints to the unrestricted coinage of silver. We do not think it necessary to go over this ground again. Whatever were the arguments for or against this step at the time it was taken, only one witness now appeared to advocate its reversal, and his advice was conditional on the attainment of a limited international agreement to maintain the price of silver. We are not in a position to say whether such an agreement could be obtained, but in any event we regard it as no longer necessary in the interests of India. As pointed out by Sir James Meston on behalf of the Government of India, much of the extra taxation imposed on India during the time when the Government were struggling against their exchange difficulties has been remitted since the rupee has been fixed on a stable basis; and with the single exception already quoted, every witness who came before us explicitly or by implication condemned the idea of a reversal of the policy of 1893 and 1898. It appears to us to be impossible to deny, in face of all the evidence, that India has derived enormous benefits from the substitution of gold for silver as the standard of value, and India's future prosperity is, in our opinion, bound up with the maintenance of the gold standard. We proceed, therefore, to the consideration of the steps which should be taken in pursuance of the policy recommended by the Committee of 1898.

9. The first principle to be borne in mind in any consideration of the Indian finance and currency system is that the balances of the

Government of India in India, and of the India Office in London, and the portions of the Gold Standard and Paper Currency Reserves located respectively in India and in London, all represent in the last analysis one single fund. The titles attached to the constituent portions of this fund indicate to some extent the nature of the needs and liabilities for which the fund as a whole is required to provide. The name attached to each portion indicates the primary function of that portion; but neither in theory nor in practice have the separate portions of the fund been entirely reserved for the objects indicated by their separate names.

10. The needs and liabilities for which these resources are required to provide may be summarised under the following five heads:—

(*i*) A working balance in India for (*a*) the current expenditure on revenue and capital account of the Imperial and Provincial Governments throughout India, (*b*) the expenditure of local boards and municipalities for which the Central Government act as banker, (*c*) the Government savings banks, and (*d*) miscellaneous funds and services such as funds in court.

(*ii*) A working balance in the United Kingdom for the "home charges" of the Government of India on revenue and capital account, including the capital outlay of most of the Indian railway systems.

(*iii*) A reserve fund for the maintenance at the par of 1*s.* 4*d.* per rupee of the exchange value of the rupee with the sovereign.

(*iv*) A fund for securing the convertibility of the notes of the Government of India.

(*v*) The provision in India of fresh supplies of coined rupees and of sovereigns as at present at the rate of one sovereign per 15 rupees.

In addition the system at present in force is used to provide facilities for remittance to India by means of Council bills and telegraphic transfers of such sums as may be required to meet the balance of trade in India's favour. This use of Indian balances is limited only by the amount of the resources available in India to meet the sales, subject, however, to the notification that bills will be sold indefinitely at 1*s.* $4\frac{1}{8}$*d.* per rupee.

11. We propose to take as the first subject for examination the currency system of India, *viz.*, the internal currency of India and the system by which a fixed rate of exchange is maintained between the media of internal circulation and the currencies of other countries which, like India, have a gold standard. The proposed mint for the coinage of gold in India, the Gold Standard Reserve, and the Paper Currency Reserve will naturally be dealt with under this section of our report. A detailed examination of the general balances of the Government of India, both in India and London,

and of the system of sales of Council drafts, will form the next section of our report.

The two next sections will be concerned with the financial organisation and procedure of the India Office and the question of the establishment of a State or Central Bank, and in the last section will be found a summary of our conclusions.

II.—INDIAN CURRENCY SYSTEM.

(1) History since 1893.

12. We shall begin our inquiry into the currency system of India by giving a summary of the main events affecting Indian currency which led up to the appointment of the Indian Currency Committee of 1898 or have taken place since the date of their Report.

13. Prior to the closing of the Indian mints to the unrestricted coinage of silver in 1893, the Indian currency system was a monometallic system with silver as the standard of value and a circulation of silver rupees and notes based on them. For the settlement of India's obligations to countries in which gold was the standard of value the rupee was exchangeable at the gold value of its silver content, and the balance of trade, then as now usually in India's favour, was settled by the import of silver bullion into India, where it could be coined at the mints into rupees at the option of the holder.

The main object of the closing of the mints to the unrestricted coinage of silver was to remedy the state of things resulting from the fall in the gold value of the rupee owing to the fall in the gold price of silver. This fall had for some time been a source of great difficulty to India, because it increased the burden measured in rupees of the external obligations of India payable in gold, while great uncertainty was introduced into the finances alike of Government and of trade by the fluctuations of exchange.

14. The closing of the mints to silver in 1893 led, as was intended, to a gradual divergence between the exchange value of the rupee and the gold value of its silver content. After a somewhat heavy coinage of rupees in 1893 the Government ceased to add rupees to the circulation. Rupees remained unlimited legal tender, and formed the standard of value for all internal exchanges. Since the Government refused, and no one else had the power, to coin rupees, as soon as circumstances led to an increased demand for rupees, the exchange value of the rupee began to rise. In 1898, soon after the Indian Currency Committee of that year was appointed, it became for the first time profitable for persons out of India who had payments to make in India to take advantage of the standing offer of the Government of India (made in 1893 in the form of a notification under an Indian Act of that year) to give rupees at the Calcutta or Bombay mints, or to issue notes at the paper cur-

rency offices, against gold tendered to them at a rate of exchange equivalent to 15 rupees for 1*l.* sterling. In short, the exchange value of the rupee had then reached 1*s.* 4*d.*

15. So long as the offer of the Government of India to give rupees in exchange for gold at 1*s.* 4*d.* per rupee remained in force and the Government were prepared to maintain a supply of rupees sufficient for this purpose, there was obviously no possibility of exchange rising above 1*s.* 4*d.* by more than the cost of shipping gold to India. But it was always possible that a falling off in the demand for currency might result in exchange dropping below 1*s.* 4*d.* by more than the cost of shipping gold from India to London, unless the Government were able and willing to give gold in exchange for rupees at 1*s.* 4*d.*, or to sell sterling exchange at a fixed rate without limit—an offer to which the Government have never in fact bound themselves.

Throughout the years 1898 and 1899 conditions favoured the maintenance of the exchange rate of 1*s.* 4*d.*, and by the end of 1899, the year in which the Committee of 1898 issued their Report, over 4,500,000*l.* of gold tendered in exchange for rupees at 1*s.* 4*d.* had been accumulated in the Paper Currency Reserve in India.

16. Such was the situation which faced the Committee of 1898. That Committee necessarily devoted considerable attention to the suggested reopening of the Indian mints to the unrestricted coinage of silver, and, in the event of the alternative policy being continued, to the consideration of the exact rate at which the exchange value of the rupee should finally be fixed. They decided against the reopening of the mints, and in favour of fixing the rupee at 1*s.* 4*d.*, and these recommendations were accepted by the Secretary of State and the Government of India. The important part of the Committee's Report for the purposes of this historical summary is therefore that which deals with the measures recommended for giving permanence to the *de facto* position in 1898-9 so far as concerns the exchange rate of the rupee.

17. The Committee had before them several schemes for giving fixity to the exchange. The scheme which they recommended was not, however, a cut and dried plan with all its details worked out in advance. They confined their recommendations to the indication of certain general principles to be followed in advancing towards an ultimate goal. What this goal was may be gathered from the following passages from their Report:—

Para. 51.—" We are of opinion that the habit of hoarding does not present such practical difficulties as to justify a permanent refusal to allow India to possess the normal accompaniment of a gold standard, *viz.*, a gold currency."

Para. 54.—" We are in favour of making the British sovereign a legal tender and a current coin in India. We also consider that at the same time the Indian mints should be thrown open to the unrestricted coinage of gold on terms and conditions such as govern the three Australian branches of the Royal Mint. The result would

be that, under identical conditions, the sovereign would be coined and would circulate both at home and in India. Looking forward as we do to the effective establishment in India of a gold standard and currency based on the principles of the free inflow and outflow of gold, we recommend these measures for adoption."

Para. 55.—"Under an effective gold standard rupees would be token coins, subsidiary to the sovereign. But existing conditions do not warrant the imposition of a limit on the amount for which they should constitute a legal tender; indeed, for some time to come no such limitation can be contemplated."

18. It is clear that the Committee looked forward to the ultimate establishment in India not merely of a gold standard but also of a gold currency in active circulation, and meanwhile contemplated an approximation to the French system of currency in which gold coins and silver five-franc pieces are alike unlimited legal tender. This involved the dethronement of the rupee within a comparatively short time from its position as the sole or principal medium of exchange and the establishment of the sovereign as an effective rival.

19. In addition to the suggestions for the attainment of this object which are mentioned in the passages quoted, *viz.*, the making of the sovereign a legal tender and the opening of the mints to the coinage of gold, the Committee recommended further (in para. 60) that "fresh rupees should not be coined until the proportion of gold in the currency is found to exceed the requirements of the public," and that "any profit on the coinage of rupees . . . should be kept in gold as a special reserve, entirely apart from the Paper Currency Reserve and the ordinary Treasury balances."

The use to be made of this reserve is indicated in the following passage (para. 59):—

> "Although the Government of India should not, in our opinion, be bound by law to part with its gold in exchange for rupees, or for merely internal purposes, we regard it as the principal use of a gold reserve that it should be freely available for foreign remittances whenever the exchange falls below specie point; and the Government of India should make its gold available for this purpose, when necessary, under such conditions as the circumstances of the time may render desirable . . . . . . and, when it has accumulated a sufficient gold reserve, and so long as gold is available in its Treasury, it might discharge its obligations in India in gold, instead of in rupees."

It will be observed that "the effective establishment of a gold standard" was the paramount object which the Committee of 1898 set before the Indian authorities. The other recommendations which we have quoted were made only because they were considered to be necessarily connected with that supreme purpose.

20. These recommendations were accepted in their entirety by the Indian authorities. It remains to consider shortly the history of events since 1899. In one respect this history is very simple. In 1898 the exchange value of the rupee touched 1*s*. 4*d*. for the first time since the closing of the mints to silver, and, except for one temporary fall to below specie point for a brief period during the crisis of 1907-8, it has remained fixed at the par of 1*s*. 4*d*. ever since.

21. This simple statement does not, however, reveal the underlying complexities of the story.

The Indian Act No. XXII, of 1899 making the sovereign and half sovereign legal tender throughout India at 15 rupees to the £ gave effect to the first recommendation of the Committee. This remains the only statutory provision for the rating of the rupee at 1*s*. 4*d*., and has the effect of providing a statutory means of preventing the rupee from rising above the par of 1*s*. 4*d*. But it is obvious that this Act does nothing to prevent the rupee from falling below 1*s*. 4*d*., and would be a dead letter if at any time it became cheaper to give 15 rupees in settlement of a debt than to give one sovereign.

22. Active steps were taken at the same date to give effect to the second recommendation, *viz*., the opening of a mint for the coinage of gold in India. The scheme was dropped after nearing completion in 1902, and has only recently been revived. But the knowledge that steps were being taken in this direction during the years 1899 to 1902 perhaps contributed to convince public opinion in India and elsewhere that the Government were determined to maintain the gold standard.

23. The third recommendation of the Committee was that the profits on the coinage of rupees should be set apart and kept in gold as a special reserve. The Gold Standard Reserve, as it is now called, is the outcome of this recommendation. By the middle of January 1900 the stock of gold in the Paper Currency Reserve in India had reached 5,000,000*l*. Though gold coins were now legal tender in India, the public continued to demand rupees, and the Government had to consider whether they should resume the coinage of rupees, for the first time since 1893.

24. The provisions of the Act of 1893 and the notification issued by the Government thereunder of their readiness to accept gold at the mints and Paper Currency Offices at the rate of 15 rupees to the £ had been supplemented in 1898 by an Act which authorised the issue at the same rate of notes in India against gold deposited in London and earmarked at the Bank of England as part of the Paper Currency Reserve. This Act was at first intended to be temporary. Its effect was to facilitate Government remittances to London, to add to the gold resources of India, and to give some elasticity to the currency by allowing of the issue of rupees or notes in India against gold tendered in London. But this additional issue of currency against gold tendered in London added to the drain on the rupee reserves of the Government in India.

25. In view of this drain, the Government of India proceeded to carry out the recommendations of the Committee of 1898 by making an active effort to induce the people of India to use sovereigns as a medium of circulation. The Currency Offices were instructed to offer sovereigns to presenters of notes, while giving rupees to any one who objected to receiving sovereigns, and at the same time the Post Offices and other institutions under Government control were utilised to press sovereigns on the public. The results were unsatisfactory. Many of the gold coins soon made their way back into Government's hands, and the Government found themselves unable to cash currency notes in rupees not only at the Cawnpore and other treasuries in the North West Provinces (where though not legally bound to do so, they had been in the habit of encashing notes), but on the 11th April 1900 at the Head Office in Calcutta itself. Notes became subject to a discount of as much as $\frac{7}{16}$ths per cent. in Cawnpore, and there was serious danger of a failure of confidence in the paper currency. Meanwhile sovereigns also went to a discount of as much as 4 annas in many places. Special demands for rupees, owing to famine conditions, and the inadequacy of the supplies of the favourite circulating medium combined to aggravate the general monetary stringency.

26. In these circumstances the Government of India resumed the coinage of rupees early in 1900 on a considerable scale. Recourse to the London silver market soon became necessary, and the Act of 1898 just mentioned was continued for a further period of two years with the addition of a provision authorising the use of the gold held in the Paper Currency Chest in London for the purchase of silver for coinage of rupees and the treatment of the silver so purchased as part of the Reserve against notes in circulation during the interval between purchase and mintage. An Act of 1902 made the whole of these provisions permanent.

Since 1900 the Government of India have not repeated the experiment of forcing gold coins into circulation, and in many years the coinage of rupees has been on a very large scale.

27. It was decided in 1900 to follow the recommendation of the Committee of 1898 and to form a special reserve from the profits on the coinage of rupees as they accrued. The Government of India put forward proposals for the formation of such a reserve in their despatch No. 302 of the 6th September 1900 (Appendix V., p. 109). Their idea seems to have been to keep the reserve in gold locked up in a special chest in India. The decision of the Secretary of State, however (as given in his despatch No. 232 of the 13th December 1900, Appendix V., p. 126), was that the profits should be remitted to London and invested in sterling securities. It was held that since London was the place in which the Reserve would have to be applied on the occasion of the emergency against which it was being created, London would be the best place in which to keep it.

28. For the first few years from 1901 onwards the profits on the coinage of rupees were accordingly remitted home by the shipment

of gold to London for investment, the gold being taken out of the accumulations in the Paper Currency Reserve in exchange for the freshly coined rupees. The interest earned on the securities purchased was also added to the Gold Reserve. These securities were at the outset Consols only, but in 1903 investments were made also in National War Loan Stock and other stocks, such as Local Loans. This extension of the area of investment seems to have been dictated at the time mainly by the desire to avoid too large holdings of one security and to earn a better rate of interest.

29. In 1905 the sterling resources of the Government of India in London were further increased by the shipment to London of 5,000,000 sovereigns out of the accumulated stocks in the Paper Currency Reserve in India, to be held as part of that Reserve in London. With a continuance of the favourable balance of trade these stocks of sovereigns had continued to increase, and the difficulties of the Government since 1899 had been, not in the direction of keeping exchange up to 1*s.* 4*d.*, but in providing sufficient rupees to meet the demands of the public, which continued to demand rupees rather than gold. The advantage of shipping these sovereigns to London and keeping them there was that they could be used there, as and when required, in purchasing silver, thus saving the three or four weeks' delay involved in shipping them from India at the moment when actually required.

30. In 1906 the same difficulty in meeting the demands for rupees led to the formation in India of a special reserve for this purpose outside the Paper Currency Reserve. At first this reserve had been held inside the Paper Currency Reserve in silver ingots, and then in partly-coined rupees, but finally in 1906 the more natural course of holding the reserve in fully-coined rupees was adopted. The fact that this reserve was needed in order to prevent the possibility of the exchange value of the rupee going to a premium over 1*s.* 4*d.* through a failure in the supply suggested that its cost might be charged against the Gold Reserve by the simple process of holding the profits on the coinage of the rupees in the Reserve in the form of rupees in India instead of converting them into sterling held in London. The name of this Reserve was thereupon changed to the Gold Standard Reserve, which thenceforward consisted of two portions, one held in sterling securities in London and the other in India in rupees.

31. Meanwhile, the practice of shipping to London gold accumulated in the Paper Currency Reserve in India, either to form part of the Gold Standard Reserve or to be earmarked in London against the Paper Currency Reserve, was recognised to be needlessly expensive. The gold, it was seen, reached India in the first place at the cost of individuals, and then had to be shipped back to London by and at the cost of Government after the public had handed it on to the Government in exchange for rupees. By an extension of the practice of receiving gold in London in exchange for rupees in India, Indian Revenues could be saved the expense

of shipping gold to London, and by the offer of remittances to the public in the form of Council Drafts could realise in the price paid for these Drafts a large part of the sums previously paid for freight and insurance on the shipment of gold to India.

32. Accordingly the practice introduced in 1898 of selling Council Drafts for gold in London and issuing notes against such gold in India was extended, and since 1904 the Secretary of State has kept open a standing offer to sell Council Bills without limit at the price of 1*s*. $4\frac{1}{8}$*d*. When the demand for these Drafts is very strong and the Treasury balances of the Government of India are insufficient to meet them, they are met by the withdrawal of rupees from the Paper Currency Reserve in India against a corresponding deposit of gold in the Currency Chest in London, and if necessary by the withdrawal of rupees from the Indian Branch of the Gold Standard Reserve. The Government meanwhile purchase silver, if necessary, in London out of the proceeds of the Council Drafts sold there and ship it to India to be coined into rupees.

33. The price of 1*s*. $4\frac{1}{8}$*d*. for Council Bills approximates to the normal gold export point from London to India, but is not at all times prohibitive of such export of sovereigns, and the India Office have not desired that it should be prohibitive; nor does it prohibit the export of sovereigns to India from Egypt or Australia. Accordingly, when sovereigns continued to accumulate inconveniently in the hands of Government in India, it was decided in 1905 to offer Telegraphic Transfers against sovereigns in transit from Egypt or Australia to India at rates of 1*s*. 4*d*. or 1*s*. $4\frac{1}{32}$ *d*., calculated to make it worth the while of the owner of such sovereigns to divert them from India to London.

34. Under these arrangements it has not since 1905 been necessary, as a general rule, for the Government of India to ship sovereigns on their own account from India to London, except in the case of light coin; and remittances for the purpose of adding the profits on coinage to the Gold Standard Reserve or for adding to the gold earmarked for the Paper Currency Reserve in London have been made by means of the sale of Council Drafts. None the less gold continues to go to India in considerable quantities in busy seasons both in the form of bullion and in the form of sovereigns, and the accumulations of gold in the Paper Currency Reserve at such times continually threaten to embarrass the Government.

35. In June 1907 a Committee appointed by the Secretary of State to consider the question of Indian railway finance recommended (in an Interim Report) that 1,000,000*l*. out of the profits on the coinage of rupees in 1907 should be devoted to the provision of additional rolling stock and other improvements for Indian railways. They were led to this conclusion by a consideration of the urgency of the need for railway development and the impracticability of borrowing the extra sum needed at that date. They justified their proposal by the following review of the strength of India's resources against a fall in exchange, which we quote as throwing

light on what may be regarded as the official view at that time of India's currency system:—

> "The object of the Gold Standard Reserve . . . . is to enable the Government of India and the Secretary of State to meet their sterling obligations in the event of a falling off in the demand for Council Bills. This reserve at the present time consists of sterling securities of the market value of 12,310,629*l.*, together with a sum of six crores of rupees (equivalent to 4,000,000*l.*) which is held in silver in India to meet any sudden demand for coinage. In addition to the Gold Standard Reserve, there is a large amount of gold (11,066,000*l.*, of which 7,705,000*l.* is held in London and 3,361,000*l.* in India) in the Paper Currency Reserve, which could be applied to the same object. Apart, therefore, from the six crores in silver, there is at the present moment a fund of upwards of 23,000,000*l.* in sterling securities and gold bullion which could be drawn upon in case of necessity."

36. The Secretary of State went beyond the Committee's recommendation and decided that for the future one half of any profits on the coinage of rupees should be used for capital expenditure on railways until the Gold Standard Reserve reached 20,000,000*l.* It was apparently contemplated that, after that total had been reached, the whole profits on silver coinage should be diverted from the Reserve. This decision was strongly criticised in India, where the recent diversion of 4,000,000*l.* of the Gold Standard Reserve from the function of maintaining exchange to the provision of a reserve of rupees had already been regarded with disfavour, and the Government of India, in a telegram dated the 24th June 1907, followed by a despatch dated the 8th August 1907 (Appendix V., pp. 158 and 160), urged that the portion of the Gold Standard Reserve held in sterling securities should be allowed to accumulate to 20,000,000*l.* before any further sums were diverted from it. The Secretary of State, however, proceeded to use 1,123,000*l.* of the profits of coinage for railway capital expenditure, and adhered to his decision as to the use of future profits. "The danger," he stated in a telegram dated the 2nd July 1907, "which you allege of a fall in exchange I regard as illusory, having regard to the present conditions of trade, the amount of securities in the Gold Standard Reserve, and of gold in the Currency Reserve."

37. The events of 1907-8, however, modified the outlook, and before any further profits on silver coinage accrued, the decision to divert part of them was reversed in 1909 (despatch No. 82 of 2nd July 1909, App. V., p. 175), and the sum of 1,123,000*l.* diverted in 1907 is all that was actually appropriated to capital expenditure.

38. The events of 1907-8 also falsified the expectations of the India Office in regard to the maintenance of the favourable conditions of Indian trade, and for the first time since the rupee was fixed at 1*s.* 4*d.*, the Gold Standard Reserve and the other sterling

resources of the Government of India had to be utilised to maintain exchange.

39. A partial failure of the summer monsoon in 1907, and the general monetary stringency all over the world which accompanied the American financial crisis in the autumn of 1907, caused the Indian exchange to become very weak in November of that year. The stock of sovereigns in the Paper Currency Reserve in India began to fall, their place being taken by rupees. The Government of India were asked by the Exchange Banks to sell telegraphic transfers on London at 15 rupees to the £, and, after consulting the Secretary of State, refused. Then the Government of India refused to give gold from the Paper Currency Reserve for export in larger quantities than 10,000*l.* to any one individual in one day, but continued to give gold for internal purposes; and as a consequence the exchange in Calcutta fell on 23rd November to as low as 1*s.* $3\frac{23}{32}$*d.* British Postal Orders for 10,000*l.* and other large sums began to be bought as a means of obtaining remittance to London. Thereupon the Secretary of State urged the Government of India to give gold for export, and being unable to sell Council Drafts, released gold from the Paper Currency Reserve in London against the transfer of an equivalent amount of rupees from the Treasury balances to the Paper Currency Reserve in India. This action, and the action of the Government of India, who, following the advice from home, consented to give out gold for export, improved exchange, which had recovered by 3rd December 1907 to 1*s.* $3\frac{7}{8}$*d.* in Calcutta. The suggestion of the Secretary of State that telegraphic transfers up to 250,000*l.* should be put up to tender by the Government in India at not less than 1*s.* $3\frac{27}{32}$*d.* was not therefore immediately acted upon, but the Exchange Banks were informed on the 7th December that the Government, in the event of serious weakness in the exchange, contemplated offering for tender in India sterling exchange on London.

40. As the normally busy season went on, rates remained weak, and the sale of Council Drafts continued impossible; finally it was decided on the 4th March 1908 to make weekly sales in India of a certain maximum quantity of sterling bills at the fixed rate of 1*s.* $3\frac{29}{32}$*d.*, instead of telegraphic transfers by tender at not less than 1*s.* $3\frac{27}{32}$*d.* as previously proposed, and on the 26th March 1908 such bills were first sold. Meanwhile the Secretary of State had taken steps to realise some of the securities belonging to the Gold Standard Reserve in order to have money ready to meet the bills sold in India. Bills continued to be sold freely in India from this date until, on 11th September 1908, the position of exchange appeared to have become sufficiently strong, and the Government of India announced the discontinuance of their offer.

41. In all, 8,058,000*l.* was withdrawn during this period from the Gold Standard Reserve to meet the bills, while a further sum of 933,749*l.* was temporarily borrowed from that Reserve and used to strengthen the India Office balances. The sale of Council Drafts in London naturally ceased during this period, but the India Office

kept themselves in funds, apart from this transfer from the Gold Standard Reserve, by the transfer of 4,530,000*l.* from the gold in the Paper Currency Chest in London (replaced, as already explained, by the addition of rupees to the Paper Currency Reserve in India) and by the issue of India Bills to the amount of 4,500,000*l.* to meet the deficit in revenue which accompanied the crisis in India. We shall return to these figures later, when considering the special question of the proper amount and disposition of the Gold Standard Reserve.

42. Since 1907-8 India has enjoyed a period of exceptional prosperity, and during this period the demand for remittances from London to India has been so strong as not only to call for the re-issue of the large stocks of rupees accumulated in India during the crisis of 1907-8, and thus incidentally to restore the Gold Standard Reserve in London to its former amount, but also to necessitate large coinages of fresh rupees in 1912-3 and 1913-4, the profit on which has gone to increase the Reserve far beyond the maximum point reached before 1907-8.

43. The only important developments affecting the Reserve since 1907-8 have been in the direction of making it more liquid. Partly owing to conditions affecting all gilt-edged stocks with no due date for redemption, and partly owing to a clearer perception of facts, the authorities responsible for the Reserve have reduced the holding of Consols and other similar securities, and have invested in preference in short-term securities, such as Exchequer Bonds and Treasury Bills. Mainly under pressure from the Government of India the Secretary of State has cancelled the decision of 1907 to divert one-half of the profits of fresh coinage, and has introduced (in 1909) the practice of holding part of the Reserve in the form of money lent out at short notice, whilst in 1912 he began to accumulate a portion in actual gold earmarked at the Bank of England. The total which the Secretary of State has expressed his intention so to accumulate is fixed at present at 5,000,000*l.* (India Office Despatch, No. 76, of 28th June 1912, App. V., p. 201).

(2) The Indian Currency System as it exists at present.

44. It will be clear from the above summary that the measures taken to maintain the exchange value of the rupee have been, to use the words of our reference, less in pursuance of the recommendations of the Committee of 1898 than supplementary to them. As already pointed out the Indian authorities duly carried out the recommendations of the Committee to make the sovereign legal tender in India, and to establish a Gold Reserve. But their first efforts to force the sovereign into circulation having failed, they abandoned the attempt actively to encourage the circulation of a gold currency in India, and, as a corollary of this change of tactics, they kept the Gold Reserve in London for use in support of exchange.

45. The investment of the Gold Standard Reserve in securities in London, the dropping of the scheme for a gold mint in India,

the practice of selling Council Drafts at something below gold point against the Currency Reserve, the establishment of the silver branch of the Gold Standard Reserve, the diversion in 1907 of money from that Reserve for capital expenditure and its use in 1908 for meeting drafts sold by Government in India on London to private traders, are all examples of divergences from the scheme adumbrated by the Committee. Thus, in spite of the fact that the Government adopted and intended to carry out the recommendations of the Committee of 1898, the Indian currency system to-day differs considerably from that contemplated by the Committee, whilst the mechanism for maintaining exchange has some important features in common with the suggestions made to the Committee by Mr. A. M. Lindsay. The system actually in operation has accordingly never been deliberately adopted as a consistent whole, nor do the authorities themselves appear always to have had a clear idea of the final object to be attained. To a great extent this system is the result of a series of experiments.

46. But to state this is by no means to condemn the action taken or the system actually in force. Indeed it is fairly certain that a too rigid adherence by the authorities since 1899 to any one preconceived course would have had unfortunate results. The experience gained from Indian experiments in currency from 1893 onwards, and the experience of British Colonies, such as the Straits Settlements, and of other countries, such as the Philippines, which have followed the Indian example, have thrown much new light on the working of currency laws. It is possible now, looking back on events in the light of this experience, to see that the present Indian system has close affinities with other currency systems in some of the great European countries and elsewhere, but it was universally believed in 1893 and 1899 that what was being done in India was an entirely new experiment.* This being so, the Indian authorities exercised a natural discretion in interpreting the recommendations of the Committee of 1898.

47. But it is desirable that, in the light of experience gained since 1898, an attempt should now be made to review and restate the principles which should guide the authorities responsible for the Indian currency system. Although the first efforts actively to encourage the use of gold in circulation in India proved a failure and have not been repeated, many people in India still regard the recommendations of the Committee of 1898 as laying down the prin-

* But *cf.* Plato, Laws, Book V., p. 742:—"[The citizens of the Ideal State] will require a currency for the purpose of everyday exchange: this is practically indispensable for workers of all kinds, and for such purposes as the payment of wages to wage-earners. To meet these requirements, the citizens will possess a currency which will pass for value among themselves but will not be accepted outside their own boundaries. But a stock of some currency common to the Hellenic world generally [*i.e.*, of international currency] will at all times be kept by the State for military expeditions or official missions abroad such as embassies, and for any other necessary purposes of State. If a private citizen has occasion to go abroad, he will make his application to the Government and go, and on his return, if he has any foreign currency left over in his possession, he will hand it over to the State, receiving in exchange the equivalent in local currency."

ciples on which the currency system should continue to be developed. We have had it in evidence from one of the non-official witnesses (*Q.* 3977) that he personally does what he can to encourage the people with whom he comes in contact to use sovereigns rather than rupees, and the evidence which we have received shows the existence of a widespread belief both in official and in unofficial circles that a gold currency in active circulation is the final goal to be aimed at.

48. The crisis of 1907-8 was the first great test to which the Indian currency system, as developed since the date of the Report of the Committee of 1898, was put, and the arrangements made for maintaining the exchange value of the rupee stood the test well. The sudden fall of exchange to 1*s.* $3\frac{23}{32}$*d.* in Calcutta in November 1907 was due, not to any insufficiency in the sterling resources of the Government but to a temporary failure to utilise those resources properly. No one in either official or unofficial circles had any experience of the machinery required for meeting the crisis, nor had any plans been fully worked out in advance for dealing with such a crisis. As may be seen from the interim report of the Indian Railway Committee of 1907 already quoted, the India Office apparently believed that the sole, or at any rate the main, purpose of the Gold Standard Reserve was to meet the requirements of the Secretary of State in London when Council Drafts could not be sold, while the Government of India made the mistake of refusing to give gold from the Paper Currency Reserve for export, though allowing their gold to be drained away for internal uses. Both authorities thus failed to recognise the wisdom of the recommendation of the Committee of 1898 that the principal use of a gold reserve is that it should be freely available for foreign remittances whenever the exchange falls below specie point. But it is fair to add that the Committee of 1898 themselves seem to have believed that a cessation of the sale of Council Drafts combined with the use of funds from the Gold Standard Reserve for meeting the requirements of the Secretary of State in London would suffice to maintain exchange, without any provision of gold by the Government for private export.

49. These mistaken ideas were, however, very quickly rectified in practice, and the steps taken to restore and maintain exchange proved adequate. It is easy to see after the event that in this or that point a mistake was made, but, regard being had to the difficulties and the novelty of the circumstances, the final success achieved by the Indian authorities both in India and in this country must be recognised as a proof of the soundness of the currency scheme itself and of the measures ultimately taken for meeting the crisis.

50. The first lesson to be learnt from the experience of the last fifteen years is that the Indian currency system has not developed on the lines of the system adumbrated by the Committee of 1898, *viz.*, a gold standard based on a gold currency in active circulation, such as the system in the United Kingdom is commonly held to be.

On the contrary it was proved in the crisis of 1907-8 that the gold in circulation in India was of very little value for maintaining the exchange. The Indian system, as the crisis of 1907-8 revealed it, is, as we have said, more like the system advocated by Mr. A. M. Lindsay in 1898, *viz.*, a gold standard supported by gold in reserve, with a currency for internal use composed mainly of rupees and notes. The chief difference between Mr. Lindsay's system and the present system is that, instead of the reserve depending mainly on the power to borrow in a crisis, an actual reserve of gold or sterling assets has been provided.

51. Experience has further shown that, though in origin and machinery the Indian currency system based on what is now known as the gold exchange standard is different from the currency systems of such countries as Russia, Holland, Japan, or Austria-Hungary, yet in actual practice these latter systems are not very different from that of India. In these countries, as in India, gold actually in circulation is of secondary importance, and the internal medium of circulation, whether it be a silver coin or a paper note, depends for its value in exchange, not on its own intrinsic worth, but on the maintenance in reserve of gold or resources readily convertible into gold, and in the case of Russia and Japan, at any rate, large portions of the gold resources are held not at home, but in London, Paris, and other monetary centres, just as India's Gold Standard Reserve is held in London.

52. A third lesson which the crisis of 1907-8 teaches is the desirability of formulating in advance and giving publicity to the policy which it is intended to pursue in a crisis. It is almost as important that the general public should have confidence in the determination of the Government effectively to use their resources to maintain the rupee at 1*s.* 4*d.*, as it is that the Government should have the necessary resources for so doing.

(3) Internal Currency of India.

(*a*) *Gold in Internal Circulation.*

53. From time immemorial India has continually absorbed the precious metals. But in quite recent years gold has been imported into India in the form of bullion or of sovereigns in greatly increased quantities. Apart from imports of gold bullion, the absorption of sovereigns by the public for all purposes (hoards, circulation, and the melting pot) during the 12 years ending the 31st March 1913, that is, the excess of the net amount imported over the amount retained in the hands of the Government, somewhat exceeded 60,000,000*l.*, an amount little less in value than the new coinage of rupees during the same period. Between the 1st April 1909 and the 31st March 1913 the absorption of sovereigns by the public was close on 30,000,000*l.* (*see* Appendix I., page 21).

54. To what extent and how widely the sovereign has established itself as an actual medium of circulation, it is difficult to

determine with any great degree of certainty. On the one hand, it is quite certain that a large portion of these 60,000,000 sovereigns is not in active circulation, and that in many parts of the country the public have shown a preference in currency uses for rupees (or notes). But there is undoubted evidence that in the last four years there has been a distinct increase in the use of the sovereign for purposes of currency in certain provinces and districts, such as parts of the Bombay Presidency and of the United Provinces, the Punjab, and Cochin in the Madras Presidency. Speaking generally, no district which wanted gold seems to have experienced in the last four years any difficulty in obtaining it.

55. In these circumstances it cannot be maintained that the public have been prevented from obtaining gold by the course pursued by the Government. On the contrary, the official policy has been to give the public whatever form of currency they wanted, and the only official preference for one form of currency over another which we can trace is, as already recorded, in favour of gold. Those, therefore, who advocate a gold currency for India, meaning by this the use of gold coins on an extensive scale for internal circulation, must take the responsibility of urging the Government of India to force upon the public more of a particular form of currency than they at present want. It may be added, at this point, that the majority of the witnesses heard by us were distinctly unfavourable to the coinage of a 10-rupee gold piece. There is little reason to believe that it would be any more popular as a medium of internal circulation than is the sovereign, while there are strong *primâ facie* objections to the introduction of a new gold coin slightly more expensive and less convenient than the sovereign, which has been gaining an ever-increasing range of general acceptability for the purpose of meeting payments outside India. On the other hand, in so far as a 10-rupee piece was successful, it would be likely to prove a more dangerous rival than the sovereign to the smaller denominations of notes.

56. Is it then desirable that the Government of India should urge or encourage the circulation of the sovereign? The chief arguments which have been adduced in favour of such action appear to be as follows:—

(*i*) That gold is a more convenient and portable medium of circulation than the rupee.

(*ii*) That a gold currency is a necessary step towards what may be regarded as the ideal currency, *viz.*, paper backed by gold in reserve.

(*iii*) That some prestige attaches to the possession of a gold currency, whereas a silver circulation is the mark of less progressive peoples.

(*iv*) That a large amount of gold in circulation is a strong, and, in the view of some people, the only adequate support for exchange.

(v) That the constant mintage of fresh supplies of rupees is objectionable, and would be obviated by an increasing circulation of sovereigns.

(vi) That until India has a gold currency in active circulation, India will continue to possess an artificial and managed currency.

(vii) That India should be encouraged to absorb gold in order to protect the world in general from a further rise of prices due to the greatly increased production of gold.

57. The first argument is valid only in so far as concerns large payments which for any reason cannot be discharged in notes; but India must continue for many years to use rupees for payment of the small amounts which form the bulk of internal transactions.

58. On the second argument we would say that history gives no support to the view that a paper currency can only be reached after a gold currency has been in circulation. A paper currency, if readily encashable, is the most economical medium of circulation, and at the same time provides a readily available reserve of gold for foreign remittances.

59. The argument that some prestige attaches to the possession of a gold currency is chiefly due, we think, to a confusion between a gold standard, which has undoubtedly become in the last forty years the mark of a progressive people, and a gold currency, in the sense of a preponderating use of gold for the purpose of effecting internal exchanges. So far as the internal circulation is concerned, a widespread use of cheques is generally agreed to be the most progressive system. After this comes the use of notes, which compose by far the greater part of the currency of most European countries. The preponderating use of gold coin is not characteristic of a single one of the Great Powers of the world, and it may be said that the only country which really conforms to this ideal is Egypt, where the continual inflow and outflow of sovereigns is an economic loss to Egypt herself and a cause of recurrent inconvenience to the money markets of the world.

60. The fourth argument, that the encouragement of a gold circulation is calculated in the long run to strengthen exchange, is probably that which carries most weight, and has been supported before us, in one form or another, by several witnesses who were in a position to speak with some authority. It requires, therefore, careful consideration.

61. In the first place, some witnesses seemed to imply that, if gold were to be used in India to the same extent that it is, say, in the United Kingdom or in Germany, the exchange problem would have been largely simplified. We think that this view is mistaken. The ability of these countries to meet at all times their immediate foreign indebtedness depends on the central reserves of the banks of these countries, on the influence exerted by these banks

on the other constituents of the money market, and on their bank rate policy. It is not possible to point to any occasion in contemporary history on which sovereigns in the pockets of the people have proved a resource on which to count for easing the situation when a monetary crisis threatens the Bank of England's gold reserve. So little are the authorities of the Reichsbank impressed by the value of gold in active circulation for the purpose of settling international indebtedness, that they have been lately engaged in an active policy of replacing some part of this gold by notes of smaller denominations than were formerly current, whilst the gold itself has been used to strengthen the central reserve. It is useless to suppose that the advantages of the existing monetary system of the United Kingdom can be obtained for India by imitating what is, perhaps, the least vital part of this system, namely, the use of sovereigns for that small class of payments which are made in actual cash, while ignoring the nature of the complex banking and financial system upon which the stability of exchange really rests.

62. In the second place, it is important that advocates of a gold currency should be clear as to the scale on which they think it would be feasible and wise to introduce such a currency in the near future. If it is their desire and their intention that gold should be used in active circulation to the same extent that it is used, for example, in Egypt, then no doubt gold from circulation would be available for export in considerable quantities at times of depressed trade. For, in that country a large part, measured in value, of the total transactions, instead of a very small percentage, as is the case both in the United Kingdom and in India, is carried out with gold, so that a contraction in the amount of business is likely to release a nearly proportionate amount of gold for export. In order to attain, however, to this state of affairs in India, or even to approximate to it, it would be necessary to reduce the note issue to a comparatively insignificant position, and to withdraw from circulation, at large expense, no inconsiderable part of the existing circulation of rupees. If, however, the advocates of a gold currency contemplate only such an addition of gold to the currency as can be made through the gradual increase of the aggregate circulation, without detriment to the existing circulation of notes or withdrawal of rupees now circulating, gold must continue to occupy for a good many years to come no more than a subsidiary position in the currency system. We do not believe that exchange would materially benefit from the circulation of gold on this scale. There would still be so many rupees in circulation that a considerable quantity could be spared at times of depressed trade, and it would be rupees which, as at present, would flow back into the hands of the Government at such times. All experience goes to show that, so long as the public have the option of making payments in tokens or in gold, it is the surplus tokens and not the gold in circulation which will seek an outlet at a time of weak exchange; and this will continue until the supply of tokens has been so far contracted that they are no more than

sufficient for the ordinary business in the transaction of which coins of a low denomination are alone convenient. Thus it is a mistake to believe that to have 10 or 20 per cent. of the total active circulation in the form of gold means 10 or 20 per cent. of the advantages, such as they are, of having nothing but gold in circulation. During the crisis of 1907-8, while 4,179,000*l*. in gold was withdrawn by the public from the Paper Currency Reserve, only 250,000*l*. was exported on private account. We do not believe, therefore, that the circulation of gold on a moderate scale only would materially reduce the liabilities which Government ought to be prepared to meet.

63. In the third place, it is of great importance to consider from what source any gold which may find its way into circulation is likely to come. If the gold merely takes the place, not of notes or of rupees now circulating, but of new rupees which it would be necessary otherwise to mint, the effect is to diminish the strength of the Gold Standard Reserve by the amount of the profit which would have been made from the new coinage. This would bring to an end the natural growth of the Gold Standard Reserve (except in so far as its present funds might be invested and earn interest), and it is very improbable that so moderate a public circulation of gold as could possibly be obtained in this way would be as valuable in supporting exchange as gold, even though of a less aggregate quantity, in the Gold Standard Reserve. But it has to be remembered that India's demand for additional currency has been exceedingly irregular; and it would be rash to base currency policy on the assumption that this demand will be large, on the average, over the period of years immediately in front of us. For if, on account of a falling off in the demand for additional currency or for any other cause, such as a greater success in the popularisation of gold than most of its advocates now anticipate, gold in circulation were to take the place of notes or of rupees now circulating, the necessary and immediate consequence of this must be a rapid depletion of the gold now held by Government in the Paper Currency Reserve. Now it must be conceded, and has in fact been acknowledged by most of the witnesses who have pressed for a gold currency, that, sovereign for sovereign, gold in circulation is less effective than gold in reserve for supporting exchange. The depletion, therefore, of the gold in the Paper Currency Reserve, which now serves as a substantial aid to the Gold Standard Reserve in the support of exchange, might gravely weaken the Government's position at a time of exchange difficulties; and the policy of popularising gold, so far from helping exchange, would have jeopardised it. Advocates of a gold currency are met, therefore, by the difficulty that the circulation of gold on a moderate scale only is of no substantial use, while, on the other hand, the circulation of gold on a large scale, at any time in the near future, must necessarily be at the expense of the existing Reserves and, so far from increasing the gold in the country, must have the effect of making what gold there is less available for the support of exchange. Advocates of this policy have

also to remember that every step in the direction of popularising gold makes it more likely that people will cling to the gold they have and seek to obtain what additional gold they can, on any occasion of crisis or general want of confidence.

64. The argument that the coinage of fresh rupees is objectionable and ought to be avoided is largely bound up with the argument just examined; for the possible danger to exchange of a very large circulation of tokens is the main ground of the objection. But this is a convenient place at which to point out that it is by no means certain that an increase of gold in circulation will be altogether at the expense of rupees. In many respects gold is a far more formidable rival to the note issue than to rupees, since for many purposes a coin of so high a value as the sovereign cannot possibly take the place of rupees, whilst experience elsewhere has shown that a public preference for gold, or alternatively for notes, is largely a matter of habit and custom. To habituate a people, therefore, to the use of sovereigns is almost certain in the long run to militate against the use of notes, even though at first the sovereign is able in some cases to obtain a vogue where, at present and immediately, this is not possible for notes. A people who have adapted their habits to the use of gold will not easily be won from them, so long as gold is easily available. Advocates of a gold currency have repeatedly told us in evidence that they by no means advocate gold in preference to notes, which they regard as a more desirable form of currency; but the policy they favour may have, nevertheless, the consequence they deprecate. There is, indeed, some evidence that the increased popularity of the sovereign in certain districts during the last two years has already hindered in some degree the growing use of notes. In his latest report (for 1912-3) the Head Commissioner of Paper Currency states (paragraph 59):—

"In paragraph 44 the conclusion has been drawn that gold has replaced rupees to a large extent in the Punjab, and to a smaller extent in Bombay and the United Provinces also. The question now arises whether the increased use of gold has affected the note circulation at all. In the Punjab it is certain that the circulation of 5 and 10 rupee notes has been affected. The gross circulation of the 5 rupee note after nearly doubling in the three years 1908-9 to 1911-2 increased by ·5 per cent. only in 1912-3. The gross circulation of the 10 rupee note in 1910-1 was more than double what it was three years before. In the last two years it has increased by 1 per cent. only. These figures considered in conjunction with the large increase in the use of sovereigns in the last two years are irresistible.

"In Bombay the gross circulation of the 10 rupee note after increasing by nearly 30 per cent. in the two years 1908-9 to 1910-1 has increased by ·6 per cent. only in the last two years.

"On the whole, it may now be definitely stated that, but for the use of gold as currency, the circulation of the smaller currency notes would have expanded much more rapidly in the Punjab, Bombay, and the United Provinces."

65. This conclusion is corroborated by some interesting figures placed before us by the National Bank of India and by the Presidency Banks as to the percentage of their receipts and disbursements at various centres in the form of notes, rupees, and gold respectively (*see* Appendix XVIII., pp. 541, 542, and Appendix XLIII., pp. 724-726). It is remarkable how uniformly in districts where the use of gold is considerable the use of notes is below the average.

66. There remains the argument that without gold in active circulation India's currency system must remain a "managed" system, it being implied that a managed system is a bad system. The ideal with which this managed system is contrasted seems to be the system of the United Kingdom where fresh supplies of the only unlimited legal tender coins, the sovereign or the half sovereign, can be obtained at will by anyone who takes gold to the mint for coinage.

In our opinion this contrast is of no value. There does not appear to us to be any essential difference between the power to import sovereigns at will and the power to have gold coined into sovereigns in India. The only point of the criticism that India's currency system is managed in a sense that is not true of the currency of the United Kingdom lies in the fact that the rupee is a token passing at a value above its intrinsic value and at the same time is unlimited legal tender. It is true that it is not practicable even to consider the limitation of the amount for which the rupee is legal tender. In this sense therefore the system must remain a managed one. But we demur altogether to the idea that because it is to this extent a managed system it must be a bad system. It is not, in fact, possible for the Government of India to manipulate the currency for their own ends, and they cannot add to the active circulation of the currency except in response to public demands.

67. With the argument that India should be encouraged to absorb gold for the benefit of the world in general we do not propose to deal. The extent to which India should use gold must, in our opinion, be decided solely in accordance with India's own needs and wishes, and it appears to us to be as unjust to force gold coins into circulation in India on the ground that such action will benefit the gold-using countries of the rest of the world as it would be to attempt to refuse to India facilities for obtaining gold in order to prevent what adherents of the opposite school have called the drain of gold to India. In any case these arguments (which it will be noted are mutually destructive) are irrelevant to the inquiry which we were directed to make and to the terms of reference, which confine us to a report on what is "conducive to the interests of India." They raise vast controversies upon subjects which are beyond our scope, while giving no reason for the adoption of either policy in India's own interest.

68. We conclude therefore that it would not be to India's advantage to encourage an increased use of gold in the internal circulation.

(b) *Proposed Gold Mint for India.*

69. It will be convenient to deal at this point with the question of the opening of a mint for the coinage of gold in India. This proposal has been recommended on the ground that it would facilitate a flow of gold to India and that the mere fact of gold being coined in India would give confidence in the permanence and stability of the policy recommended by the Committee of 1898. Both these considerations have lost much of whatever weight they originally carried. Gold has flowed freely to India in recent years without this stimulus and we doubt whether any more could have been attracted by mere facilities for coinage.

70. Nor do we believe that the opening of such a mint would be of value at this date in winning public confidence in the stability of the exchange value of the rupee. This consideration had its force in 1899 and 1900, but the experience of 1907-8, the growth of the Gold Standard Reserve, and the whole trend of policy and opinion since 1898, leave no doubt as to the determination of the Government to maintain exchange, and in so far as confidence in their power to do so is lacking, it must be secured by measures which will make a real and not merely an imaginary addition to the resources available for this purpose.

71. More recently the idea of a gold mint has been pressed on the ground that it would increase the amount of gold in circulation. Even if we thought this in itself desirable, we are unable to follow the supposed connection between the end in view and the means recommended for securing it. The people of India can obtain under present conditions as much gold as they desire for currency purposes. Indeed the more usual difficulty is that gold coin is in greater abundance in the Reserves than is required for internal circulation. But even if this were not so, the mere existence of a mint for the coinage of gold could not add to the amount of gold available for currency purposes, and the idea that such a mint would give India an "automatic" currency, in any sense which is not true of the existing power to import sovereigns at will appears to us to be wholly without foundation.

72. Nor is it likely that the facilities for converting gold bullion into coin which such a mint would provide would have any appreciable effect on the amount of gold withdrawn from circulation or would encourage gold to come out of hoards in unfavourable seasons. It is quite true that at times of famine and distress gold must come out of hoards, but we see no reason for believing that the amount so forthcoming would be increased by the opening of a mint for gold. The public in any case would secure equal advantages if the Government of India were to renew the notification, withdrawn in 1906, of their readiness to receive refined gold at the Bombay Mint in exchange for notes or rupees.

73. In our opinion, if this were done, it would remove the only practical grievance which can be alleged against the present system in this respect and would render wholly unnecessary the opening

of a mint for the coinage of gold. We recognise however that there is in some quarters a strong, though a by-no-means unanimous wish, that such an opening should take place. The authority of the Committee of 1898 can be cited in its support and there is said to be a strong sentiment in its favour. We find it difficult to judge accurately of the depth and extent of this feeling. For the reasons already given we do not ourselves share it and we cannot recommend on its merits the establishment of a gold mint in India. But if Indian sentiment genuinely demands it, and the Government of India are prepared to incur the expense, there is, in our opinion, no objection in principle either from the Indian or the Imperial standpoint, provided always that the coin to be minted is the sovereign (or the half-sovereign); and it is pre-eminently a question in which Indian sentiment should prevail. If, however, the final decision be against the opening of a gold mint, we recommend that the notification of the Government's readiness to receive refined gold at the Bombay mint should be renewed on suitable terms.

(c) *Conclusions.*

74. We have already stated that it is not to India's interest that further efforts should be made to encourage the circulation of gold as currency. We regard gold in circulation as wasteful, and we think that India should be encouraged to develop economical habits in matters of currency. In dealing with the paper currency system of India we shall make some suggestions in this direction, and any improvements in the banking facilities of India which tend to discourage the wasteful habit of hoarding the precious metals will be of great value to India. But while educating the people in the use of more economical forms of currency, it is important that the Government should continue to act on the principle of giving the people the form of currency for which they ask. We recognise that for many years to come a metallic currency will be the only suitable one for the vast majority of transactions in India, where over 90 per cent. of the people are illiterate and cannot be expected to use paper notes or cheques to any considerable extent.

75. There will still be opportunities for the use of gold coins rather than rupees in circumstances in which notes are not suitable and rupees are inconveniently cumbrous, and there will necessarily remain for a long period a considerable demand for gold coins for hoards of all kinds until the habit of banking takes the place of the hoarding habit as a means of securing and increasing savings. The line between gold in hoards and in circulation is an indefinable one, and the hoarding habit is sanctioned by the experience of centuries in India and by religious and racial laws and customs, with which the Government of India have neither inclination nor power to interfere. Any attempt to refuse gold to meet these legitimate demands would be unjust and foredoomed to failure, and could only cause alarm and instability. The proper line of advance consists not in actively discouraging the use of gold for currency but in encouraging the use of notes.

76. To sum up, our view is that India neither demands nor requires gold coins to any considerable extent for purposes of circulation (as opposed to saving or hoarding), that the most generally suitable media of internal circulation in India are at present rupees and notes, and that the Government should, as opportunity may offer, encourage notes, while providing—and this is the cardinal feature of the whole system—absolute security for the convertibility into sterling of so much of the internal currency as may at any moment be required for the settlement of India's external obligations.

(4) Gold Standard Reserve.

77. What then are the sterling resources of India for providing for the payment of India's external obligations? These resources consist of the Gold Standard Reserve, of the part of the Paper Currency Reserve held in gold or sterling securities, and of the India Office balance. This balance is, however, in normal conditions not more than is needed for working purposes, and may, therefore, be disregarded in any review of the resources permanently available to support exchange in a time of crisis.

78. We have already given a summary of the development of the Gold Standard Reserve since the date of its first inception. The principal criticisms directed against it as at present administered are to the location of the greater part of it in London, to its amount, to its composition, and in particular to the presence in a fund formerly designated the Gold Reserve and now the Gold Standard Reserve of a considerable sum in silver.

79. The experience of 1907-8 makes it clear that the Reserve is required not merely to meet the "home charges" of the Government of India at a time when an adverse rate of exchange prevents the free sale of Council drafts, but also to liquidate an unfavourable balance of trade to the extent necessary to prevent exchange from falling below specie point. On the other hand, the Reserve is not required to provide for the conversion into sovereigns of the rupees in circulation in India. Gold is world's money, and India, like other great countries, needs gold less for internal circulation than for the settlement of external obligations when the balance of trade is insufficient to meet them. That being so, the aggregate amount of rupees in circulation has only an indirect bearing on the question of the Gold Standard Reserve. It is true that the Reserve is built up out of the profits on the coinage of rupees, but its object is not to secure the convertibility on demand of the whole of the rupees in circulation but only to provide a reserve sufficient to convert into sterling such amount of rupees as may at any moment seek export; in other words, such amount as the owners require to exchange for sterling in order to settle debts due in sterling.

80. This being the purpose of the Reserve, its amount depends not so much upon the amount of rupees at any time in circulation as upon the growth of India's trade and the extent of the deficiency which adverse seasons or circumstances may at any time be reason-

ably expected to produce in the country's power to liquidate immediately its foreign obligations.

81. The total amount up to which the Reserve should be accumulated has been a much canvassed question from the first. Our view that the amount depends upon India's trade balance implies that there is no need to accumulate the Reserve beyond the point at which it will be sufficient together with other sterling resources to meet all reasonably probable requirements in a time of adverse trade. But this point is not capable of exact definition. As trade expands and wealth increases in India imports will expand as well as exports. But the larger the total volume of the trade the larger is the amount (though not necessarily or even probably the proportion) of the possible variation from year to year in the net balance in favour of or against India. If the habit of private investment in sterling securities were to assume considerable proportions, and if India had already invested largely in such securities, the consequent possession of large sterling assets by the public in India would in itself act as a reserve for the support of exchange.

82. But for the present the growth of trade and industry carries with it a continual increase in the possible demands on the reserve fund in adverse times. One of the most noticeable features in the crisis of 1907-8 was the fact that for some time after the crisis had declared itself imports from abroad, ordered in advance in times of prosperity, continued to pour into India, thus accentuating the adverse conditions resulting from the failure of the crops and the consequent falling off in the volume of the exports. This must always be the case, and the larger the trade the greater will be the adverse balance which by these circumstances may be created. The failure of the crops and the consequent reduction of exports are sudden in their origin and immediate in their effect. Exports fall at once, but imports continue to flow in under outstanding orders and cannot be checked till those orders are exhausted. In time the balance would restore itself, but in the meantime exchange would have collapsed. It is to maintain exchange in the interval before the balance of trade can right itself that the Reserve exists, and its resources must be sufficiently liquid to be used at once and sufficiently large to meet the most prolonged strain to which it may reasonably be anticipated that they might be exposed.

83. There is normally a very large net balance of trade in India's favour; but in the year from 1st November 1907 to 31st October 1908 the imports of merchandise, including gold and silver, exceeded the net exports by 1,190,000*l*. (*see* Appendix IV, p. 108). Such an occurrence in the case of India, with an expenditure of 20,000,000*l*. a year on revenue account, apart from capital outlays to meet in London, indicates the necessity for a very large sterling reserve, and the fact that this net excess of imports over exports of 1907-8 followed on a net balance in India's favour of 31,010,000*l*. in the corresponding twelve months of 1906-7 shows the enormous extent of the fluctuations to which India's trade is liable. The fact that in this particular instance the balance was righted by the issue

of gold (or sterling assets) to the extent of 18,000,000*l.* in London and India combined cannot be taken as a measure of the amount which might be required under different circumstances and with a larger trade.

84. The crisis in question was undoubtedly a severe one. Its main features were a failure of the summer monsoon and a partial famine, coincident with a world-wide financial crisis. But the famine was not the worst experienced in India, the failure of the monsoon was for one season only, and the storm centre of the world-wide crisis was in New York and not in London. It is impossible therefore to take the crisis of 1907-8 as a measure of the maximum demand on the Reserve. A second failure of the monsoon in the following year would undoubtedly have added to the burden, even though the check upon imports and the effect upon prices resulting from the previous year's crisis would have done something to mitigate its evil consequences, whilst, if the storm centre of the crisis had been in London, the difficulty of realising large quantities of the securities in which the Reserve was then held might have been considerable.

85. We do not accept, therefore, the figure of 18,000,000*l.*, which was the measure of the demand made by the crisis of 1907-8 upon the sterling reserves of the Indian Government, as an adequate guide to the amount which may be required in a similar crisis in future. Experience of a second period of adverse exchange is necessary before it will be safe to prescribe with any degree of precision the proper magnitude of the aggregate sterling reserves.

86. There remains the question what part of the burden of supporting exchange ought to fall on the Gold Standard Reserve and what part on the gold in the Paper Currency Reserve. It is the declared intention of the authorities at present to increase the Gold Standard Reserve up to a total of 25,000,000*l.*, and then to reconsider the necessity of continuing to appropriate to it the whole of the income from its present sources of supply. Of the Paper Currency Reserve the gold earmarked in London (at present 6,100,000*l.*) is commonly regarded as a far more reliable support to exchange than the gold held in India, and as the part of which account ought primarily to be taken. We incline to the view that reliance ought to be placed on gold in the Paper Currency Reserve for the support of exchange only in so far and so long as the Gold Standard Reserve is not yet adequate to support the burden by itself. There is no great likelihood of this in the immediate future and we do not think, therefore, that it would be useful for us to attempt to lay down at present any hypothetical limit beyond which additions to the Gold Standard Reserve should cease. We are accordingly of opinion that, even after allowance is made for the earmarked gold in the Paper Currency Reserve, the suggested total of 25,000,000*l.* is insufficient.

87. Our unwillingness to set a limit to the accumulation of the Gold Standard Reserve, so far as this is due to profits on the coinage of rupees, is increased by the fact that otherwise Government may

appear to lay themselves open to the charge that they can (if foreign exchanges be left out of consideration) provide themselves with as much money as they like for internal expenditure by the simple process of coining rupees without limit. We do not suggest that it is even conceivable that the Government of India would actually take this suicidal course. But at the same time it appears to us undesirable that any Government should be open to attack in this way if it is possible to avoid it.

88. And here it may be well to notice the suggestion made by one witness that the Gold Standard Reserve has been built up by means of great sacrifices on the part of the revenues of India. The word "sacrifices" appears to us to be out of place in this connection. In building up the Reserve India has not sacrificed revenue. The most that can be said is that revenue has not been artificially swollen by the appropriation in aid of ordinary expenditure of certain funds which were rightly and necessarily devoted to a special purpose.

89. While, therefore, looking beyond the immediate future, we hold that the Government of India ought to be alive to the possibility of the aggregate sterling reserves eventually reaching an unnecessarily high figure, we recommend that the whole profits of the silver coinage, together with any interest accruing from investments or loans made from the Gold Standard Reserve, should for the present continue to be placed to the credit of that Reserve, and that no diversion similar to that made in 1907 for railway development should be under any circumstances permitted until further experience allows of a much more accurate definition of the calls which the Reserve may have to meet than is at present possible.

90. The most suitable place for the location of the Gold Standard Reserve is, in our opinion, undoubtedly London, and in this view the majority of our witnesses concurred. London is the clearing-house of the world, India's chief customer is the United Kingdom, and London is the place where money is required both for the expenditure of the Secretary of State on India's behalf and for payment of India's commercial obligations to this country and the world in general. If the Reserve were kept in India it would have to be shipped to London to be used. This would involve delay at a moment when immediate action is essential. The objections put forward to keeping it in London rest on the belief that the Reserve is regarded in London as being available to supplement the Bank of England's reserve. There is no foundation at all for this belief. We have no hesitation therefore in recommending that the whole of the Gold Standard Reserve should be kept in London.

91. It remains to consider the composition of the Gold Standard Reserve. We have already mentioned the fact that until recently the whole of the London portion of the Reserve was kept in securities, and none in gold. Circumstances have profoundly changed since 1899 when the Indian Currency Committee were able to speak naturally of keeping a reserve in gold without proceeding to consi-

der whether " gold " meant sterling securities or actual gold. At that time it scarcely occurred to anyone to distinguish between Consols and cash. The crisis of 1907-8 resulted in the sale of a large part of the Consols and similar securities held on account of the Reserve. It was fortunate that these securities were disposed of with little difficulty and without greatly reducing their market price. It may be regarded as a further piece of good fortune that it was necessary to dispose of these securities at that date and that the fund was therefore not affected by the further depreciation in their capital value which has since occurred. Larger quantities of short-dated securities less liable to capital depreciation were acquired when the Gold Standard Reserve again accumulated, and the cost price of the Consols and similar securities actually held on the 31st March 1913 was only 5,886,280*l*. out of investments the cost of which was 16,906,561*l*. in all.

92. The Secretary of State had so far yielded at the latter date to the arguments of the Government of India as to hold 1,005,664*l*. in loans at short notice, and a sum of 1,620,000*l*. in gold earmarked at the Bank of England, this latter sum being the beginnings of a total sum of 5,000,000*l*. which he is gradually accumulating in this form.

93. We are of opinion that the actual gold held in the Gold Standard Reserve should stand at a much higher figure than 5,000,000*l*. In the existing circumstances of the London money market even the finest securities such as Consols can no longer be regarded as identical with cash in the sense in which they were so regarded fifteen or twenty years ago, and their realisation might involve such a loss in capital value and such an aggravation of a crisis which it would be India's direct interest to allay, as to make the holding of more than a comparatively moderate proportion of such stocks undesirable in the case of the Gold Standard Reserve. Short term securities such as Treasury bills, Exchequer bonds, and similar securities have this advantage over Consols that the chance of any big loss of capital on realisation is less; but these securities may not be always realisable in large amounts quite so quickly or readily as Consols, and their enforced realisation at a particular moment might, under certain circumstances, so aggravate an adverse situation in London as to increase India's difficulties and to injure Indian interests. In so far as such securities as Consols continue to be held in the Gold Standard Reserve, we would call the attention of the authorities to the consideration that to obtain an advance against such securities by pledging them might in some cases be a preferable alternative to selling them outright, since it might be possible to raise money in this way after it had become difficult to sell except at a very serious loss.

94. In any case, the realisation in a crisis of securities in large quantities, and even the calling in of sums lent out at short notice, are likely to cause some stringency in the London market, and if the exchange crisis in India which makes such realisation necessary is accompanied or directly caused by a financial crisis in London or

reacting upon London, as is very probable, the difficulty of realisation may be accentuated, and the possibility of loss to India cannot be ignored. India should, in this respect, be as far as possible independent of London. Just as London must look to its own resources in such a crisis, and does not and cannot count on help from Indian reserves, so India should be in a position to defend its own financial position without undue recourse to the gold reserves of London. The Gold Standard Reserve is built up out of the fruits of the economy of gold. It is a necessary condition of such economy that an adequate reserve should be held against an exchange crisis, and it is right that such reserve should be sufficient in itself to meet the crisis and should not be dependent on conditions which India cannot control or on resources accumulated by another country to meet its own liabilities.

95. What then is the amount of actual gold which should be held on account of the Gold Standard Reserve? We do not think that it is possible to fix an amount which will hold good for all time. The amount of actual gold depends like the aggregate of the whole fund on a consideration of conditions which are constantly changing. We see no necessity for keeping the whole fund in gold, as is sometimes demanded. To do so would be, in our opinion, unnecessary and wasteful, and would take away from the Reserve an important source of future increase. On the other hand, we are clearly of opinion that the actual holding of gold in this Reserve has been and is insufficient, and that it is important to take immediate steps for its increase.

96. In our opinion, the best rule in present circumstances would be that not less than one-half of the fund should be held in actual gold when the total fund exceeds 30,000,000*l*., and that a minimum amount of 15,000,000*l*. should be accumulated as rapidly as possible. If this rule is followed and a sum of not less than 5,000,000*l*. is usually kept in gold in London as a part of the Paper Currency Reserve, it will be possible for India in a time of exchange crisis to release in actual gold an amount equal to the amount of securities which it may be desired to realise, and at the same time to have a final reserve of gold left. So soon as circumstances render recourse to the Gold Standard Reserve necessary, the policy of the authorities should be to use both the securities and the gold, advantage being taken of the release of gold to facilitate the realisation of securities.

97. Taking the figure at the 31st March 1913, the total amount of the Gold Standard Reserve was:—

	£	£
Securities at market value . .	15,945,669	
Money lent at short notice . .	1,005,664	
		16,951,333
Gold deposited at the Bank of England . .		1,620,000
		18,571,333
Silver in Indian Branch: 6 crores at 1*s*. 4*d*. .		4,000,000
		22,571,333

98. The holding of silver in the Gold Standard Reserve has given rise to much criticism, and is responsible for much confusion and doubt as to the efficiency of the Reserve. If the proposals which we make in a later section in regard to the Paper Currency Reserve are carried out, it will be possible to exchange at once the 6 crores of silver for 4,000,000*l*. of gold, and we recommend that this should be done. Further, the Paper Currency Reserve will be able to take over from the Gold Standard Reserve at least 4,000,000*l*. of its securities in exchange for gold.

99. These transactions will at once raise the total amount of gold in the Gold Standard Reserve from 1,620,000*l*. to 9,620,000*l*. This figure is still much below the proportion suggested by us.* It should be further increased as opportunity offers for the revision of existing investments as well as by the addition of new money.

100. The gold transferred from the Paper Currency Reserve in India might continue to be held there for a time as part of the Gold Standard Reserve, but, as we are of opinion that London is the proper place for the Gold Standard Reserve, steps should be taken to transfer it to London as soon as convenient.

101. We have considered whether it would be desirable to make the Gold Standard Reserve the subject of statutory regulations. But there are disadvantages in restricting the freedom of Government in a crisis, and it is undesirable that the disposition and amount of the Reserve should be stereotyped until further experience makes it possible to forecast with greater certainty the nature and the extent of the calls which may be made upon it. We therefore do not recommend that the Gold Standard Reserve should be regulated by statute. But we advise that the Government should make a public notification of their intention to sell bills in India on London at the rate of 1*s*. $3\frac{29}{32}$*d*. whenever they are asked to do so (as was actually done in 1908, and confirmed in 1909), to the full extent of their resources. We believe that the knowledge that such exchange can be purchased at any time will do much by itself to inspire confidence, and so to reduce the actual demand for drafts on London, and to prevent that feeling of panic which is liable to accompany and to aggravate periods of financial strain. With the Reserve for the support of exchange so strong as it will, we hope, prove if our recommendations are accepted, we do not think that there is any reason to fear that in undertaking this liability the Government of India would be in any danger of being unable to carry out their obligations.

(5) Paper Currency.

102. The Government Paper Currency System of India dates from 1862, in which year the previously existing notes of the Presidency Banks, which had only a restricted circulation, were withdrawn, and a Government monopoly of Note issue was established.

* The figure 1,620,000*l*. is that of the gold held on the 31st March 1913. Considerable additions have been made to this total quite recently, while this Report has been under discussion.

The notes are in the form of promissory notes of the Government of India, payable in rupees to bearer on demand, and are issued in denominations of 5, 10, 50, 100, 500, 1,000, and 10,000 rupees. They are issued without limit at any paper currency office against rupees or gold. For the purpose of the note system, India is divided into certain circles, and (with the exception of the 5-rupee note which was universalised outside Burma in 1903) the notes were, until 1910, legal tender only within the circle of issue, and could be encashed as of right only at the head office of the circle of issue. In 1910 power was taken to make the notes universal legal tender throughout India and encashable as of right at the head offices of each of the circles, now seven in number, and under this power all the smaller denominations of notes up to and including those for 100 rupees have been universalised. Extra-legal facilities for encashment are given at most of the Government treasuries, and, in practice, notes are freely encashed there within reasonable limits. The growth of the gross circulation was slow. From 3·69 crores in 1862 it had reached only 15·77 crores in 1890. After that date the increase was more rapid, and of late years especially since the partial abolition of the circle system, the circulation has expanded very fast. The figures are (in crores of rupees):—

Average of Year.	Gross Circulation.	Notes held in Reserve Treasuries.	Net Circulation.	Notes held in Government Treasuries other than Reserve Treasuries.	Notes held in Presidency Bank Head Offices.	Active Circulation.
1900-1	28·88	2·34	26·54	1·81	2·68	22·05
1906-7	45·14	3·66	41·48	1·99	5·56	33·93
1911-2	57·37	5·53	51·83	2·34	7·60	41·89
1912-3	65·62	10·71	54·92	2·52	7·01	45·39

103. The Indian system of note issue was avowedly modelled on that of the Bank of England as regulated by the Bank Charter Act of 1844, and in its main features remains unaltered to this day. It was provided in 1862 that a metallic reserve should be kept against the whole of the notes issued with the exception of such amount not exceeding 4 crores of rupees as might be fixed by the Governor-General in Council with the consent of the Secretary of State. This amount was to be invested in Government securities. The amount of the Reserve that may be invested has been increased by special Acts from time to time to 14 crores, of which a maximum of 4 crores may be held in sterling securities. The composition of the Reserve on the 31st March 1913 was as follows:—

Total Circulation.	Silver in India.	Gold in India.	Gold in London.	Securities.	
				Sterling.	Rupee.
Crores.	Crores.	Crores.	Crores.	Crores	Crores.
68·97	16·45	29·37	9·15	4·00	10·00

It will be seen that the securities now amount to a little over 20 per cent. of the total reserve. In spite of an addition of two crores to the securities in 1911, this is a much lower percentage than was usual in earlier years, the figures at the end of each year in which the successive additions to the securities have been made being—1871-2, 44·9 per cent.; 1890-1, 27·2 per cent.; 1896-7, 42·1 per cent.; 1905-6, 26·9 per cent.; 1911-2, 22·8 per cent.

104. In this country the intention of the framers of the Bank Charter Act of 1844 was to prevent the abuses attendant on the issue of notes without the backing of a metallic reserve by securing the retention in reserve of coin against every single note issued over and above a maximum amount which was allowed to be covered by securities. This system was for long believed to be the ideal of a note issue system. But in fact its result has been to reduce notes to a very insignificant position in the British Currency system. The complete inelasticity imposed by the Act of 1844 upon the currency of notes, an inelasticity which can only be modified temporarily and as a last resort by the extra-legal power assumed by Government of suspending the Bank Charter Act in a crisis, has only been tolerated because of the discovery in the cheque system of an alternative means of obtaining an elastic paper currency, which could not be obtained through the note issue under the terms of the Act. The main paper currency of the United Kingdom now consists of cheques, and the gold reserve of the Bank of England, though nominally supporting a comparatively small note issue, is really the ultimate support of a gigantic currency of cheques and other credit instruments of which the notes of the Bank of England form only a small portion.

105. In India, at all events outside the Presidency towns, conditions have not as yet favoured any great extension of the cheque system or of credit instruments generally, and metallic currency and notes of small denominations remain the favourite and the only suitable currency medium with the vast majority of the public. But since the closing of the Mints to silver in 1893, the expansion in the trade and commerce of India has made the need for a more elastic currency increasingly felt, and the restrictions imposed upon the note issue system by the requirement of a metallic backing for all notes issued above a fixed maximum, which can only be altered by a specific Act of the legislature, have become increasingly inconvenient. Some elasticity has, it is true, been introduced, rather incidentally than intentionally, by the Gold Note Act of 1898 and the development of the system of sales of Council Drafts already referred to (para. 24), under which it has become possible for notes to be issued in India against money tendered to the Secretary of State in London. But so far as the Paper Currency system itself is concerned this elasticity is secured only by the earmarking of gold in London, which is equivalent to the export of gold from London to India; the expansion of the currency of India is thus at the expense of the gold reserves of London, and in some circumstances the resulting stringency in London is so disadvantageous

to India as to make an expansion of the currency by this means actually undesirable.

106. Before considering the possibility and desirability of adding elasticity to the note issue system we must first examine, more particularly, the present location and disposition of the Paper Currency Reserve.

In our summary of events relating to the exchange value of the rupee we have explained how it came about that this Reserve was made a part of the machinery for receiving gold, both in India and in London, in exchange for rupees, for holding in India gold intended to be passed into circulation, and for acting "as a first line of defence," as it has been called, for the 1*s*. 4*d*. parity of the rupee. While the main object of the Reserve is to secure the absolute convertibility of the notes, the location of the Reserve and the proportion between the gold and silver in the metallic portion now depend on other considerations as well.

107. The holder of a note is entitled to receive payment for it in Indian legal tender money, that is in sovereigns, half-sovereigns, or rupees. As he usually prefers rupees and has a right to demand them, the first necessity is that sufficient rupees should be held in the Reserve to meet this demand. To meet demands from this and other causes during the busy season the Government consider that the stock of rupees in reserve should not be allowed to fall below 24 crores on the 1st November in any year, or 18 crores on the 1st May in a year of active trade (see question 9099). These figures have been evolved on the basis of experience and are periodically reconsidered. As six crores are at present held in the Gold Standard Reserve the minimum figures for the Paper Currency Reserve are 12 crores on the 1st May, and 18 crores on the 1st November. If the outflow during the busy season is so great as to threaten a reduction below 12 crores on the 1st May, or the inflow during the slack season is insufficient to build up a total of 18 crores on the 1st November, steps are taken to coin fresh rupees.

108. The total amount of gold in the Paper Currency Reserve naturally fluctuates inversely with the total stock of rupees in the same Reserve. When the rupees threaten to fall short, the gold accumulates, and it is by using the excess gold that the cost of silver for fresh coinage is eventually met. As already explained, the authorities endeavour, through the sale of Council Drafts in London, to secure that the gold should not accumulate in India to such an extent as to involve shipment back to London. In practice the amount of gold accumulated in India has, except when depleted by the exchange crisis of 1907-8, always tended to exceed the maximum demand for gold from the Reserve in India. The policy pursued in quite recent years has been to locate from about five to seven millions sterling in London, and only to secure the presence in London of further gold belonging to this Reserve when the money is wanted to purchase silver. This policy has been criticised by some of the witnesses who appeared before us. It seems to us, however, to be at present justified by two considerations. In the

first place it is reasonable that for the purchase of silver some part of the Paper Currency Reserve gold should be kept in London, as the principal source of supply: for this purpose no great amount is required. But, second, there is the maintenance of exchange to be considered. The facts are that the gold in the Reserve in India has been much in excess of the demand, that the Gold Standard Reserve has not in itself been sufficient to secure beyond question the stability of exchange, and that gold in London is more directly and indubitably effective for this purpose than gold in India. In these circumstances, so long as the Gold Standard Reserve is insufficient by itself for the support of exchange, we think the policy is justified.

109. The present maximum for the securities in the Reserve is, as already stated, 14 crores. Until 1905 the whole of the securities held consisted of rupee paper, but the additions of two crores in 1905 and two crores in 1911 have taken the form of investments in sterling securities. This extension of the area of investment was made, partly with the object of not having too large holdings of a security which was likely to be depreciated by the same causes as would possibly entail a run on the Paper Currency Reserve involving their sale, and partly as an additional sterling support for exchange.

110. We are of opinion that considerable improvements can be made in the location and disposition of the Paper Currency Reserve.

In the course of our inquiry the suggestion has frequently come up for consideration that the Gold Standard and Paper Currency Reserves should be amalgamated. The overlapping which occurs between the functions of the two Reserves makes this suggestion attractive, and it is possible that an amalgamation may be found desirable in the future. But for the present we think that the balance of advantage lies in the maintenance of two separate Reserves.

A very conservative treatment of the Gold Standard Reserve may, however, in certain circumstances strengthen the position of the Paper Currency Reserve. A drain on the Gold Standard Reserve for the support of exchange alters, not its volume, but only its form; and when rupees have accumulated in this Reserve, as a result of providing gold for payments abroad, these rupees are available, if necessary, for transfer to the Paper Currency Reserve in exchange for sterling securities. Such a transfer would be financially sound from the point of view of both Reserves; and, provided that the rupees were only issued from the Paper Currency Reserve in exchange for notes previously circulating, the total reduction of currency would be no less than before. In the consideration of the Paper Currency Reserve, therefore, the increase of strength which would accrue to the Gold Standard Reserve, if our proposals under that head are adopted, ought not to be entirely overlooked.

111. We have already recommended that the six crores of rupees in the Indian Branch of the Gold Standard Reserve should be hand-

ed over to the Paper Currency Reserve, which is the more natural place for keeping a reserve of rupees. The minimum figures of 24 crores on the 1st November and 18 crores on the 1st May for the stock of coined rupees in reserve will be unaffected, but in future this stock will be entirely within the Paper Currency Reserve. 4,000,000 sovereigns should concurrently be transferred from the Paper Currency Reserve in India to the Gold Standard Reserve.

112. Our next recommendation is that the fiduciary portion of the Paper Currency Reserve should be increased at once to 20 crores. But instead of merely fixing this figure as a maximum, we propose that the maximum of the fiduciary portion should be fixed at the amount of the notes held by the Government in the Reserve Treasuries *plus* one-third of the net* circulation for the time being. Under this proposal the invested portion of the Reserve will be at once increased by six crores. We recommend that this result should be effected by a transfer (at market value) of sterling securities to that amount from the Gold Standard Reserve in exchange for six crores of the gold now in the Paper Currency Reserve in India.

113. So long as the gross circulation exceeds 60 crores, it will be within the power of the authorities to increase the investments of the Reserve and we propose that the Government should have power not only to make such further permanent investments as they think fit but also to make temporary investments or to grant loans either in India or in London. In India such loans should be made to the Presidency Banks on the same terms as we propose hereafter in the case of loans from balances, while in London the Secretary of State should have power to lend out in the London market sums received in payment for Council Drafts sold against the Currency Reserve in the busy season so long as the total of the cash portion of the Reserve does not fall below two-thirds of the net circulation.

114. We hope for the following advantages from our recommendations: (1) While the permanent addition to the invested portion of the Reserve will be no more than is justified by past practice and experience without in any way endangering the complete convertibility of the notes, the revenues of India will secure the profit earned by investing the amount now held idle in the form of gold in India. (2) There will be occasions, especially in the busy season, when it will be safe to lend temporarily sums which it would be unwise to invest permanently. The power to make such loans will, therefore, enable the Government to earn interest on sums which would otherwise lie idle needlessly, and will provide at the same time a much needed facility for a temporary expansion of the currency in the busy season, by virtue of which the market may obtain some relief, though not at first, perhaps, a very great amount, from its recurrent stringency. (3) The power to make temporary investments in London on account of the Paper Currency Reserve will be a convenience to the Secretary of State in permit-

*By net circulation we mean the gross circulation less the amount of notes held in the Reserve Treasuries, *cf.* para. 102.

ting him to sell Council Drafts against the Paper Currency Reserve, in anticipation of silver purchases or of any other cause, without the loss of interest and other disadvantages which might sometimes come about if he were compelled, without discretionary power, to utilise the entire proceeds of such sales in earmarked gold. (4) As the circulation of notes in India increases, it will be within the power of the authorities to increase as and when desirable either the permanent or the temporary investments of the Reserve or both without a special Act. (5) The power to make loans from the cash held against notes in the Reserve Treasuries will provide the Government with a useful alternative or supplementary means of counteracting some of the disadvantages arising from the existing Reserve Treasury system with which we deal in the next section of our report.

115. We think it eminently desirable that the use of notes in India should be encouraged by all legitimate means. With this object in view, we recommend that the Government should increase, whenever and wherever possible, the number of places at which the notes are encashable as of right as well as the extra-legal facilities for encashment. We think it would be desirable to universalise at once the notes of 500 rupees. With the experience so gained it may be found possible to carry universalisation still higher. We do not think that the extra cost of remitting specie from place to place to provide for the encashment of notes would, except at the outset, be appreciable, and we think that, in any case, it would be more than counterbalanced by the advantage of an increased circulation of the notes as a medium of currency.

116. In accordance with our general view as to the position of gold in the internal currency of India, the gold remaining in the Paper Currency Reserve in India will be used for meeting demands in India just as at present. The Government will not undertake to supply gold in all circumstances, but should be ready in normal times to supply gold for internal purposes up to the full extent of the resources of the metallic portion of this Reserve. But, as soon as an exchange crisis declares itself in the form of an effective demand for bills on London at *1s.* $3\frac{29}{32}$*d.*, any gold in the Paper Currency Reserve in India should be given out only on such conditions as will secure its immediate export.

117. The amount of gold held at any time on behalf of the Paper Currency Reserve in London will be regulated according to the conditions of the metallic reserve in India. When rupees are plentiful and the stock of gold correspondingly small in India, the Secretary of State will hold not more than the amount of 5,000,000*l.* which we have allowed for as the normal amount of actual gold likely to be available in London outside the Gold Standard Reserve in support of exchange. In a time of crisis this sum of 5,000,000*l.* should be treated, not as the first line of defence for the exchange, as it has sometimes been called, but as standing behind the Gold Standard Reserve, especially the gold portion of it, so far as ex-

change is concerned, while serving also the important function of acting, together with and in support of the sterling securities in the Paper Currency Reserve, as a final resource for securing the convertibility of the notes in an internal crisis in India. Any additions to the gold held on account of the Paper Currency Reserve in London over and above the sum of 5,000,000*l*. should be regarded as temporary only, and used as and when required for the purchase of silver for coinage into rupees, the function of such additional gold being to maintain the internal currency of India and not to support exchange.

118. The following tables show in parallel columns the position of the Gold Standard and Paper Currency Reserves on the 31st March 1913 and the position as it would have been on the assumption that our recommendations had been carried out at that date, and will explain at a glance the effect which our recommendations would have upon the location and disposition of the Gold Standard and Paper Currency Reserves.

GOLD STANDARD RESERVE AT 31ST MARCH 1913.

Sterling:	Market Value.
	£
Securities not due for early redumption . . .	4,956,165
Securities due for early redumption	10,989,504
Sums lent out at short notice . .	1,005,664
Total invested .	16,951,333
Gold deposited at Bank of England .	1,620,000
Total in London .	18,571,333
Rupees in India:	
Rupees in reserve in India, 6 crores, equals . . .	4,000,000
Grand Total .	22,571,333

GOLD STANDARD RESERVE AS PROPOSED BY COMMISSION.

	£
Securities not due for early redemption (say) . .	2,456,165
Securities due for early redemption (say) . .	9,489,504
Total invested .	11,945,669
Gold	*10,625,664
Grand Total . .	22,571,333

Of the gold the greater part would at first be held in India, but would be replaced as circumstances permitted by gold earmarked at the Bank of England.

*Viz.:—

	£
Gold already held . .	1,620,000
Gold received for securities transferred . .	4,000,000
Gold received for rupees transferred .	4,000,000
Gold realised by calling in short loans .	1,005,664
	10,625,664

Paper Currency Reserve at 31st March 1913.

	Crores.	Crores.
Rupees	...	16·45
Gold in London	9·15	
Gold in India	29·37	
		38·52
Securities at cost:		
In London	4·00	
In India	10·00	
		14·00
Gross circulation	...	§68·97
Amount of Notes in Reserve Treasuries	...	12·68
Net circulation	...	56·29

Paper Currency Reserve as proposed by Commission.

	Crores.	Crores.
Rupees	...	†22·45
Gold in London	9·15	
Gold in India	‡17·37	
		26·52
Securities at cost:		
In London	†10·00	
In India	10·00	
		20·00
		68·97

The maximum fiduciary portion being one-third of net circulation	=18·76		
plus Notes in Reserve Treasuries	=12·68		
		31·44	
And the actual investments being		20·00	
There was available for temporary investment or loans			11·44

Total Amount of Gold in London as at 31st March 1913 in Gold Standard and Paper Currency Reserves combined as proposed by Commission.

	£
In Gold Standard Reserve (assumed to be all in London)	10,625,664
In Paper Currency Reserve (in London)	6,100,000
Total	16,725,664

†6 crores transferred from Gold Standard Reserve.

§At this date the gross circulation was exceptionally large.

	Crores.
‡ Gold already held in India	29·37
Deduct—	
Transferred to Gold Standard Reserve in exchange for rupees and securities	12·00
	17·37

III.—BALANCES.

(1) Aggregate Balances.

119. We have now disposed of the questions of currency which we had to consider and pass to the second, or, as it may be called to distinguish it from what precedes, the financial branch of our inquiry. This has relation to the moneys of the State, and includes the amount and location of the Government balances as well as

the method by which their distribution between London and India is arranged, that is to say, the system of Council Drafts.

120. In view of comparisons which are sometimes made between the total balances kept by India and by the Government of the United Kingdom, it is desirable to begin by drawing attention to the danger of basing arguments upon any such comparison. The general balances of the Government of India and the India Office balances do not correspond in any way to the Exchequer balance at the Bank of England as shown in the statement of revenue and expenditure published in the "London Gazette" of Tuesday in each week. They correspond more closely with the Government deposits as shown in the weekly statements of the Bank of England; but even here the comparison is inadequate, as the Indian Government's balances both in India and in London include considerable sums held on behalf of Indian railway compaies, sums belonging to local and district boards for which the Government act as bankers, and many other items, for which no close parallel can be found among the items which go to make up the British Government's deposits at the Bank of England. The Indian total, also, includes large sums held as working balances at the various treasuries and sub-treasuries throughout India and Burma, as well as the balances at headquarters in India and in London, whereas, except for the small balance kept at the Bank of Ireland, the British Government keep practically only one working balance and that in one place only, *viz.*, at the Bank of England. For all these reasons arguments founded on a comparison of the total balances of the two Governments must be used with great caution.

121. The next step in this part of our inquiry must be to determine the amount which it is essential for the Government to hold in London and in India respectively.

122. We are advised that the minimum working balance required in London is normally about 4,000,000*l.* and looking to the large payments that fall due at the beginning of each quarter, we consider that this amount is not excessive. In India the standard balance is very much higher. The minimum balance, we have been told, with which the Government of India can work their transactions, is about 8,000,000*l.*; this minimum is reached normally in November or December; and, since between April and the end of the year there is a large net withdrawal from the Government treasuries, it is the practice to budget for an opening balance in each financial year of something over 12,000,000*l.*

123. This estimate of requirements is based on experience, and we have no reason to doubt its accuracy. It has naturally not been possible for us to examine in detail the working of the "Resource Operations" of the Government of India, that is, the machinery for keeping the various treasuries and sub-treasuries in India in funds, nor have we the knowledge required for undertaking such an examination. It is, however, clearly desirable that any Government should endeavour by all reasonable means to manage their

collections of revenue and the amount of their balances from time to time in such a way as to cause as little inconvenience as possible to the money market. We therefore call attention to the importance of a periodic review by the Government of India of the amounts so held in order to secure all possible economy of balances and to take advantage of all fresh facilities for remittance which the growing development of communications and other modern improvements provide.

124. We have indicated that the normal figures for the closing balance each year are, in London 4,000,000*l.* and in India 12,000,000*l.*, making in all about 16,000,000*l.* Compared with these normal figures, the actual balances have been in recent years:—

31st March.	In London. £	In India. £	Aggregate. £
1908 . . .	4,607,266	12,851,413	17,458,679
1909 . . .	7,983,898	10,235,483	18,219,381
1910 . . .	12,799,094	12,295,428	25,074,522
1911 . . .	16,696,990	13,566,922	30,263,912
1912 . . .	18,390,013	12,279,689	30,669,702
1913 . . .	8,783,970	19,293,131	28,077,101

125. The great excesses shown by these figures have naturally attracted attention, and in particular the very large balances which have been held in London have been the subject of much adverse comment. It will be clear, however, that the primary factor has been an excess in the aggregate of the Government moneys, which alone made it possible for the London balance to be so much above the normal. It is this factor, accordingly, that we propose first to examine, and we shall then proceed to deal with the distribution of the aggregate, and the location of a great part of it in London.

126. The first point to be noted is that the great rise in the balance as a whole has not been in accordance with the anticipations of the Government; on the contrary, each budget has provided for a reduction of balances to a figure not far removed from the normal, and each year the intentions of the budget have been defeated by an improvement in revenue or by a falling off in expenditure which were not foreseen at the time of its preparation. It would seem, therefore, that primarily the question is one of estimating, and we cannot but feel that in preparing their estimates of revenue the Government of India have erred on the side of caution. We are convinced, however, that, in the peculiar circumstances of India, this is an error on the right side, and that the consequences of too sanguine a forecast, perhaps committing the Government to premature expenditure beyond their real resources, and involving at any time the risk of a deficit, are much more serious than those which can arise from the occurrence of large surpluses. In the circumstances of such a country as India it is not safe to spend up to the hilt during a period of prosperity; there is everything to be said for a general policy of caution which utilises the increased resources of such a period to strengthen the financial position against the

recurrence of bad seasons, and it is certain that the adoption of this policy in recent years has done much to secure Indian finance against vicissitudes in the immediate future. It is to be remembered also that in recent years the position of the opium trade, which hitherto has contributed largely to the Indian revenues, has been altogether exceptional. So uncertain in fact have been the prospects that recently the Government of India have deliberately estimated the receipts under this head at the figure which they were likely to reach under the least favourable circumstances, while specifically hypothecating in advance any surplus that might accrue over that figure to certain particular kinds of expenditure.

127. A further cause of the large figures reached by the aggregate balances has been the failure to spend up to the amount estimated on capital account. This feature is particularly noticeable in the year 1910-1, when over 3,000,000*l.* out of a total estimated outlay of 6,500,000*l.* in India remained unspent at the end of the year, and over 1,000,000*l.* was similarly left unspent in London out of a total of 6,250,000*l.* Much of the underspending is attributable to the Indian railway companies rather than to the Government authorities in London and India. Several witnesses have drawn attention to the general question of Indian railway finance, and have urged the importance of a settled programme of railway development, providing for three or four years in advance. The adoption of such a plan, if properly followed up in other respects, should undoubtedly reduce the underspending, but except in this connection this subject has appeared to us to fall outside the scope of our reference. Whatever the ultimate reason for this underspending may be, it is an important contributory cause to the size of the balance, because the probability of underspendings only becomes known late in the financial year, whereas the borrowings of the India Office to meet such expenditure have usually taken place some time earlier.

128. In the circumstances of the case we recognise that cautious estimating was in the main justifiable, though it was carried rather further than was necessary. Even under normal conditions we have been much impressed by the difficulties of preparing a budget in India. The revenues of India, whether shown under railways or customs or directly under the head of land revenue, fluctuate to an extraordinary extent with the success or failure of the agricultural operations of each year, and these again depend predominantly on the south-west monsoon which spreads over the Indian continent and Burma in the months of June to October. Under present arrangements the Indian budget is presented before the end of March, and the Finance Minister accordingly has to prepare his estimates in ignorance of the most important factor on which the results of the year will depend. The late Finance Member of the Viceroy's Council, indeed, has described the framing of a budget as a gamble in rain. We would observe, however, that the description applies only because the budget is taken before the monsoon. It is clear in fact that from the financial point of view the present date is

almost the most inconvenient possible for the budget, and the suggestion has therefore been made that the date of the beginning of the financial year should be altered from the 1st April to the 1st November or 1st January. There may be administrative difficulties in carrying this suggestion into effect, but, financially, it would be a great improvement. Criticism directed against the inaccuracy of Indian budgetting is not effectively answered by a reference to the difficulties which arise under present conditions. It has to be shown further that these difficulties cannot be removed by a change of date without incurring graver disadvantages, and we commend the question to the consideration of the Government.

129. When the excess of the aggregate balances is mentioned, however, the criticism which we have elicited from witnesses has been directed, not so much against the inaccuracy of recent budget estimates, as against the continuance of taxation which, it is alleged, was in fact unnecessary. With this second criticism we have in the circumstances no sympathy. If the budget anticipations had been more in accordance with results, it is true that they would have shown much larger surpluses, and they might have suggested the possibility of a reduction of taxation. But there are peculiarly strong reasons in India against temporary alterations in the scale of taxation, and it is clear that the finances of the country were faced in the near future by two circumstances, first the disappearance of the opium revenue, and second the inception of a large programme of new expenditure particularly on education and sanitation, which made it extremely improbable that a reduction of taxation, if sanctioned, could be maintained for any length of time. In the circumstances it was clearly better to follow the policy which was in fact adopted of making use of the additional resources provided by a period of prosperity, not for the reduction of taxation, but for the general strengthening of the financial position.

(2) Location of Balances.

130. We now pass to the question of the location of balances, a subject which has aroused much criticism. Government money, it is said, has been moved unnecessarily from India where it would have assisted business, and the London money market has had an accession to its resources at the expense of the country to which the money primarily belonged. To the extent of the normal working balances the location of Government funds has already been determined, and it is only the excess over these amounts which has now to be considered. With regard to this excess there are two principles to be observed. The first is that it is undesirable financially that a Government should borrow with one hand and lend with another; so that the first object to which any surplus should be applied is the reduction or avoidance of debt. The second principle is concerned with the relations of Government to the trader and the general taxpayer. It is implicit in the criticisms we have noticed that it was the duty of Government to help trade in India, but it

is not clear whether in the opinion of the critics this should have been done even if it resulted in a loss of revenue in the shape of interest or in some other form detrimental to the general welfare represented by Government. On this point there can be no doubt that it is the general welfare that has to be preferred. It may be admitted that the Government should in money matters adapt themselves as far as possible to the requirements of trade, but they must clearly subordinate the interests of particular classes to the welfare and security of the whole.

131. We will endeavour to apply these principles to the recent conditions of India. If there is a debt outstanding which can be paid off, London is the place where a surplus balance should be located. The same considerations apply if avoidance be substituted for reduction of debt. As far as the ultimate object is concerned, therefore, to which a surplus balance should be applied, we hold that it must come to London. So far, we understand, the critics of Government would agree, but they add that the balances were transferred to London prematurely and in advance of requirements. Granting then that the final application of surplus balances was satisfactory, the question which arises is one of their intermediate investment. This, on the second principle indicated by us, would appear to depend primarily upon the relative security and rate of interest obtainable in India and in London respectively; in other words, if the security were as good and the rate were as high in India, the Government would be well advised to keep their surplus money there; but, if the security were better or there were a prospect of earning more in the London money market, they should transfer their funds to this country.

132. In the circumstances of India, however, these are not the only factors to be considered. The surplus balances now under consideration naturally arise in periods of prosperity, when not only the revenues of the Government but the claims of India against other countries are expanding, and exchange is high. It is natural that the Government should take advantage of these conditions to transfer their money to London at a favourable rate of exchange, and the possibility of a loss in exchange if they defer action has always to be set against any advantage they may gain meanwhile by lending out their money in India at a higher rate of interest. Whether, therefore, we are considering the final or the intermediate employment of any surplus balance, it will be seen that strong reasons exist for transferring it to England.

133. We find no fault, therefore, with the course, taken by Government in recent years, for, under the conditions hitherto laid down for loans in India, there was no effective demand for such loans and no use for the money in that country. If, however the recommendations which we make as regards loans in India be approved, there will be new opportunities for the temporary use of a portion of this money in India, and the occasions, though not the extent, of transfer may have to be revised accordingly.

(3) Indian Balances.

134. We now proceed to an examination of the balances held in India. The balances of the Government of India in India are divided between the district treasuries and sub-treasuries, the branches of the Presidency banks, the head offices of those banks at Calcutta, Bombay, and Madras, and the Reserve Treasuries at these three places. The following figures showing the distribution on the 31st March 1912 illustrate the normal position of these balances at the close of the financial year:—

	£
In 270 district treasuries (including some 1,500 sub-treasuries)	5,790,700
In 36 branches of the Presidency banks . .	1,580,500
At the three head offices of the Presidency banks .	1,402,500
At the three Reserve Treasuries	3,506,000
Total	12,279,700

135. Certain fixed minimum sums are kept at the head offices of the Presidency banks under agreement with the Government, *viz.*:—

	£
At the Calcutta office of the Bank of Bengal . .	233,300
At the Bombay office of the Bank of Bombay . .	133,300
At the Madras office of the Bank of Madras . .	120,000
	486,600

These minima may be regarded as (speaking generally) part of the remuneration to the banks for work done for Government and compensation for the loss in 1862 of the privilege of issuing notes. In practice the Government of India keep considerably larger sums at these head offices, *viz.*:—

At Calcutta, 467,000*l* to 533,000*l*.
At Bombay, 267,000*l*. to 333,000*l*.
At Madras, a little over 133,000*l*.

136. Branches of the Presidency banks are regularly used for the keeping of the Treasury balances in the comparatively few places where such branches exist, and the Government have made a practice of late years of offering to guarantee a fixed minimum balance for a period of five years as an inducement to the banks to open new branches and take over the district treasuries in the places where such branches are opened. But, except in places where such a guarantee is in operation, Government balances at the branches of the banks seldom exceed immediate requirements to any considerable extent, the Government's policy being, as a general rule, to draw any surplus balances to certain centrally situated treasuries and finally to the Reserve Treasuries. The balances at the head offices of the Presidency banks are not allow-

ed to exceed certain fairly well-defined maxima, except temporarily and for special reasons. Thus, in practice, whatever surplus Government balances there may be in India at any time tend to be accumulated in the Reserve Treasuries.

137. The independent Treasury system is not an ideal one, and compares unfavourably with the practice prevailing in the United Kingdom and in most other countries of keeping Government balances at a bank. In the United Kingdom, as in India, a considerable proportion of the total revenue is collected in the first four months of the calendar year. The heavy collections of revenue which then take place undoubtedly have a considerable effect on the money market, but the trouble is minimised in two ways, first because the money collected is immediately deposited at the Bank of England, where it is available for financing the commerce of the country; and, second, by the device of Treasury bills for supply and ways and means, ways and means advances and deficiency advances, which enable the Government to tide over the lean period of the year by borrowing from the market sums which they repay as revenue accrues later on, thus maintaining some sort of equilibrium in the demands of the Exchequer upon the cash supplies of the nation. This is a device not practicable in India, where the resources of the money market are as yet too limited to enable the Government to rely on financing themselves through the lean months by borrowing. In India, therefore, the minimum balance of the Government must be sufficient for their wants and the money collected as revenue is necessarily under present conditions taken off the market and immobilised in the Reserve Treasuries.

138. The disadvantages of the system are accentuated by the special conditions of India, where business is subject to a seasonal tide of strongly marked character. That business it will be remembered is predominantly agricultural, and all the principal crops, whether jute or rice, cotton or wheat, or oil seeds are marketed in the autumn and winter. Thus every year there is a busy season with active trade and great demand for money, and a slack season when money frequently cannot be lent. Something of the same sort occurs also in the affairs of Government; and far more than the proportionate amount of the revenue is collected in the first few months of each calendar year. We have noted that the minimum balance is reached in November or December. From that point the balance begins again to rise, and by the end of March is normally 4,000,000*l.* higher than in December. This season of maximum collection of revenue coincides with the season of busiest trade, and thus it happens that, at the time when the market stands most in need of funds, the Government are taking off the market a sum of 6 or 7 crores not for the sake of immediate requirements but in order to meet disbursements during the slack season of the summer and autumn.

139. The figures of the closing balances in India on the 31st March 1913 are instructive in this connection. Instead of the

normal balance of about 12,000,000*l.* the total balance was 19,268,200*l.*, which was distributed as follows:—

	£
In 270 district treasuries	6,590,500
In 35 branches of Presidency banks	2,198,300
In 3 head offices of Presidency banks	1,595,600
In 3 Reserve Treasuries	8,908,700
	19,293,100

Close on 9,000,000*l.* was thus locked up from the market in the Reserve Treasuries as compared with about 3,500,000*l.* a year before, while only 3,752,100*l.* out of the total of 19,268,200*l.* was placed with the banks. Only a comparatively small portion of the 2,198,300*l.* deposited at branches of the banks can be regarded as readily available in the money market, but as this money would for the most part necessarily be located in much the same places under any system, it may be counted as being at any rate more available for trade than if it had been in district treasuries. The causes which led to this state of things on the 31st March 1913 were mainly a sudden slackening off in the demand for Council drafts, unaccompanied by any noticeable slackening of internal trade in India, and a record surplus of revenue over expenditure. It appears to us that a system which leads in certain circumstances to the locking up of nearly 9,000,000*l.* during the busiest period of the commercial year, and 5,400,000*l.* more than under the same system was similarly locked up in the previous year, requires very strong justification.

140. We have said that Government cannot sacrifice the interests of the general taxpayer to the interests of trade. Nevertheless, we should be the first to recognise the immense importance of trade to the prosperity of the country and the revenues of Government. The principles now observed result in loans being granted from Government balances only in exceptional circumstances, and while there is a provision that Presidency banks may retain on payment of interest sums in excess of those which it is the practice to leave with them, this provision appears to have had little publicity and has not been acted upon. In effect we may say that the assistance rendered by Government to trade has so far been confined to the amount left at the headquarters of the Presidency banks.

141. At the same time there are those who hold that the disadvantages of the Indian system have been exaggerated. Two points must here be noted.

142. In the first place the view has been expressed that the bank rates ruling in India are not after all excessive. During the busy season these rates generally rise as high as 8 per cent., and in some years they have remained at that figure for a considerable time. Occasionally they have risen even higher. But this

does not mean that the average bank rate in India is high. On the contrary, it is possible for firms and individuals who can offer good security to borrow money all the year round at an average rate of interest very little, if at all, higher than would be charged for similar accommodation in the United Kingdom. In these circumstances it is argued that there is no real ground for complaint and that trade can easily afford the higher rates of the busy season.

143. This view was expressed to us by several witnesses, including the representatives of the Exchange banks, but it was not generally shared by other witnesses. There is much to be said for the complete neutrality of Government in such matters, but complete neutrality, by which we mean the absence of influence one way or the other on the rates for money, is not practicable in India in present circumstances. The action of Government undoubtedly helps to create the annual stringency, and there is therefore at least a *prima facie* case for such counteraction as is possible to relieve it.

144. Second, it is said that the stringency in the Indian money market, so far as it is caused by the withdrawal of money by Government, is relieved by the sale of Council drafts, which again place the surplus held by Government at the disposal of trade. This is largely true, but it omits some factors of considerable importance. The demand for money arises in the first place from the necessity of financing the movement of crops up country, but Council drafts are taken only when the produce is ready for export; there is thus an important period during which the needs of the market are not met by this means. It is obvious also that the sales of Council drafts are affected by circumstances quite independent of the Indian money market; a high bank rate in London, for instance, or the holding back of produce in India for higher prices, may result in the demand for Council drafts being slack in the busy season, while revenue collections are as heavy as ever. In this case the money so collected accumulates in the Reserve Treasuries and remains locked up there. As an illustration of this effect we may point to the experience of last cold weather, to which we have already alluded, when there was a marked falling off in the sales of Council drafts, with the result that enormous sums accumulated in the Indian balances and at the same time the bank rate was high in all three Presidencies. Finally, even when Council drafts are being freely sold, a temporary surplus, as we have observed, is left in India during the closing months of the financial year which is not immediately required for Government purposes; and as far as this temporary surplus, at any rate, is concerned, the argument that the sale of Council drafts relieves the stringency caused by the action of Government has no relevancy.

145. We arrive, therefore, at the conclusion that the present methods of dealing with balances are open to criticism, and we proceed to consider what remedies can be suggested for the evil of which complaint is made. For the purposes of this inquiry it seems desirable to review the discussions which in the past have

centered round the utilisation of the balances in India. From 1863 to 1876, the whole of the Government balances at headquarters were handed over to the Presidency banks. On one or two occasions, however, the Government were not able to obtain on demand the free use of the balances deposited with the banks, and the difficulties which they experienced led in 1876 to the establishment of the Reserve Treasuries. It was felt that a Government exposed in a peculiar degree, as the Government of India undoubtedly are, to sudden demands and unforeseen contingencies could not afford to lose control of their balances, and in addition it was urged that the system which was about to be superseded was wrong in principle. "Capital supplied by Government," observed the Secretary of State, "and not representing the savings of the community is a reserve on whose permanence no reliance can be placed.........a political exigency withdraws the adventitious resource, and the commerce which trusted to it finds itself pledged beyond what its own resources can make good."

146. On the other hand, it must be mentioned that, in the correspondence which led to the establishment of Reserve Treasuries, the same authority said that it would be open to the Finance Department in India either to retain the reserve in the Treasury or lend it out for short terms on suitable conditions as to interest and security. The question of Reserve Treasuries and of loans from Government balances has been a subject of discussion from time to time ever since. In 1888, the Bombay Chamber of Commerce raised definitely the question of loans by Government in the busy season, pointing out that the Treasury balances are at a maximum at precisely the period of greatest demand for funds. The Government, however, held to the position which they had taken up in 1876; they referred to a paper by Sir James Westland, to show that their balances were not excessive and that the method of dealing with them was sound; trade, they thought, should depend on its own resources and systematic advances by Government in the busy season would tend to reduce the working balances of the country to an unsafe minimum with consequent risk of panic, to guard against which was an important object of the Reserve Treasuries. If advances were made below the published rate, they added, it would be difficult to confine the privilege of obtaining Government money to the Presidency banks; these banks would be tempted to speculative operations with State resources, allowing their own resources to fall below the limit of safety. The conclusion of Government, therefore, was that they should confine any assistance from the Treasury to loans through Presidency banks at the published rate of interest in relief of temporary stringency.

147. In 1898 the Bengal Chamber of Commerce renewed the proposal, pointing out that the question was not one of wholesale surrender of Treasury funds to the Presidency banks, but the discretionary disposal of them in periods of stringency. On this occasion the proposal had better success with the Government of India, for after some hesitation they proposed to the Secretary of

State that it should be recognised as part of the ordinary business of management of the Treasury balances to lend money to the Presidency banks at 1 per cent. less than the declared minimum rate of interest during the months of January to May of each year. The Secretary of State, however, was unable to accept the recommendation of the Government of India. The effect, he thought, would be to interfere with the remittance to England at a favourable rate of exchange of the amount necessary for the discharge of the sterling obligations of Government—a point on which we have already touched and to which we shall return. Any general understanding of the kind proposed he added would induce trade to lean even more than it had done in the past on the assistance of Government instead of taking steps to enlarge the amount of loanable capital in the country. The grant of loans in India accordingly was made subject to the retention by Government of an amount sufficient to meet not only their disbursements in India but the probable amount of remittances to England. On this condition loans were permitted, but the Secretary of State thought that they should not as a rule be made below bank rate, and this rule in fact has been followed ever since by the Government of India. Our opinion on the various points raised in this correspondence will appear from what follows.

148. The most obvious solution of the problem would be to close the Reserve Treasuries and to place the whole of the Government balances in Calcutta, Bombay and Madras, with the head offices of the Presidency banks there, or, if the Government attach great importance to having a reserve immediately under their control, it might seem enough to fix a maximum total, (say) 1,000,000*l.* or 2,000,000*l.*, to the amount to be held in the Reserve Treasuries, and to place the remainder with the banks. The banks would naturally be called upon to make a suitable payment to Government for such additional privileges.

Such a change would involve a reversal of the action taken in opening the Reserve Treasuries in 1876 and the following years. It does not, however, necessarily follow that the action then taken was injudicious. The Presidency banks have enormously expanded their business in the interval, and the proportion of Government deposits to private deposits would be very much smaller now than in 1876.

149. It remains true, however, that if this solution were adopted the proportion of the Government deposits to those of other customers would still be much larger than is usual in the case of any European Government, and there is certainly danger in allowing the somewhat restricted money market in India to rely too much on the use of Government funds. Moreover other difficulties would arise: for the Treasury balances and the Paper Currency Chests are closely inter-connected in the resource operations of Government throughout India; and there are some important questions as to the provision of funds in India for meeting Council drafts also to be considered in this connection.

150. The alternative to the closing of the Reserve Treasuries is that Government should make loans from their balances. This is the course which we recommend on the understanding that the amount of the loans is within the absolute discretion of Government, and that they are made only on good security and for short periods. At the end, however, of a discussion which has lasted for more than 30 years, the Government are not in the possession of any effective system of making such loans and the question is clearly one which deserves the most careful consideration.

151. It appears to us that this proposal has been prejudiced in the past by a failure to distinguish it from other proposals which we do not favour. This is clear from the correspondence of which we have given a resumé. The general argument which Lord Salisbury, as Secretary of State, used in his despatch of 6th May 1875 (Appendix II., page 32), against the use of Government funds as permanent capital, was relevant and effective against the system which till then was in force, of making over the central balances permanently to the Presidency banks, but it was employed at a later date by the Government of India as a reply to a suggestion for temporary loans during the busy season. Similarly in dealing with the same proposal when made by the Bengal Chamber of Commerce in 1898, Sir James Westland went back to the radical differences between English and Indian conditions which justify the Government of the United Kingdom in keeping their balances with the Bank of England, but make it unsafe for the Government of India to keep all their money with the Presidency banks, and he again suggested that the proper cure for stringency during the busy season in the Indian money market was the increase of banking capital. These considerations do not apply to the scheme which we are now contemplating.

152. The arguments which are still urged against the grant of loans in India are put forward partly in the interests of Government and partly in the interests of trade. The main arguments which are based on the interests of Government are two in number. In the first place it is said that the contingencies and sudden demands to which the Government of India are subject are so numerous that they cannot safely make loans out of their balances. It is true that the circumstances of the Government of India are such as to require a policy of great caution in financial administration. But the loans which we contemplate will not depirve the Government of the use of any portion of their balances for more than a short period, and they will be made only in the discretion of Government, and we cannot agree that the argument applies to loans of this kind.

153. Again, it has been urged that the policy of granting loans in India may interfere with the remittance of Government funds to England at the most favourable rate. To this argument it might be sufficient to reply that it is clearly not applicable in all circumstances; we need only refer once more to the conditions of the cold weather of 1912-3, when the demand for Council drafts

was smaller than usual and it is clear that the question of exchange did not enter into the problem of disposing of the Indian balances. For such cases it seems essential that the Government should retain discretion to grant loans.

154. But we would go further, and suggest that even under normal conditions the problem of exchange may not present such difficulties as are sometimes anticipated. What is in the minds of those who urge this objection is that the grant of loans from the Indian balances will reduce the demands for Council drafts in the busy season when exchange is at its highest, and that, consequently there will be a loss when the Secretary of State finds that he has to draw money to London at a less favourable season. It appears to us, however, that the effect of such loans cannot be to reduce the aggregate amount of Council drafts sold; at the most, it can result only in a shifting of the sales from one part of the year to another, and it is not clear that, if the exchange in consequence falls at one time, it will not be correspondingly improved at the other. To a certain extent, the number of bills might increase at the expense of telegraphic transfers, since the first are used more largely in the slack, and the second in the busy season; but against any slight loss caused in this way would have to be set the interest earned in the meantime on the Indian loans. The last Financial Statement of the Government of India noticed the tendency shown in recent years for the busy season to encroach on the slack, and this tendency would probably be strengthened by any reduction in the price of money in India during the months of heaviest demands. On this point, however, we have no wish to dogmatise, and we content ourselves with saying that, in our judgment, there is nothing in the exchange question which would justify the Government in a general policy of refusing loans in all circumstances.

155. On the other hand, there are two distinct advantages which the Government forego when they refrain from making loans. The first is the interest which would be earned on any surplus balance which may be held in India in excess of immediate requirements. The second is concerned with the permanent loans which Government raise yearly in the Indian market, with which we deal later.

156. The argument against the grant of loans in India which is based on the interests of trade is that the Treasury balances of the Government are a very uncertain quantity, that consequently the assistance rendered to trade by loans from these balances would be spasmodic, and that inconvenience or worse might result if on occasion it were necessary for Government to refuse the assistance to which trade had become accustomed. If it is sought, however, to apply this argument to temporary loans during the busy season, we are not impressed with its cogency. When that season of the year is reached, the results of the monsoon have been established and the Government can calculate the financial prospects for the next few months with considerable accuracy. Nor is it to be supposed that the continuance of the same amount of assistance year

after year would be taken for granted. The progress of the revenue and expenditure of the Government is well known to the public; the banks themselves could generally forecast whether the Government were likely to be in funds. The outlook would be discussed from time to time by them with the Government, and they would not base their arrangements on the assumption that they would receive a loan wihout some assurance that the money would be available. The unexpected indeed may always intervene and the derangement of plans in that case would certainly prove inconvenient both to the Government and to the commercial world; but it does not appear to us reasonable that the fear of such a contingency should deprive the market year after year of the surplus funds of Government.

157. It was, however, in view of this objection that several witnesses made proposals for loans from the Paper Currency Reserve as a preferable alternative to loans from balances, on the ground that loans could be made with safety from that Reserve at times when the Government happened not to have surplus balances in India. There is a very close connection between the two alternatives, because the greater part of the amounts locked up in the Reserve Treasuries usually consists of Government notes. The figures for the 31st March 1912 and 1913 respectively were:—

		Amount in Reserve Treasuries.		Amount of Notes.
		£		£
1912	—	3,506,000	. . . . (5·18 crores)	3,453,000
1913	—	8,908,000	. . . . . (12·68 crores)	8,453,000

Thus, 5,000,000*l*. out of the extra 5,402,000*l*. located in the Reserve Treasuries on 31st March 1913, as compared with 31st March 1912, consisted of notes. As the fiduciary portion of the Paper Currency Reserve has hitherto been a fixed amount, the result of accumulation of a surplus balance in India has been to lock up an approximately equal amount of metallic currency in the Paper Currency Reserve.

158. It would accordingly make no practical difference to the Indian money market whether loans were made from the balances or from the Paper Currency Reserve, if the amounts lent were the same; and provided that due precautions are taken we think that both sources may be used for the purpose of loans. We therefore recommend that the Government should declare their willingness to grant loans from balances in India when it is in their power and interest to do so. We proceed to define the conditions and terms under which we think loans might be given.

159. There are three different ways in which the grant of a loan may become possible. In the first place, as already pointed out, the Government in the ordinary course hold an unemployed balance in India, namely, the difference between the true minimum working balance of November or December and the figure to which the balance is raised by the additions made to it from then on-

wards during the busiest months of the year, and there is no reason why normally some or all of this surplus, according to the circumstances of the time, should not be placed at the disposal of trade. Second, it may happen, as in the early months of 1913, that the Government of India's balances expand far beyond their usual dimensions; and here again it seems of distinct advantage to the parties concerned that Government should lend as much as they prudently may and as much as the commercial community can utilise. Finally, while recognising that the first duty of the Government is to secure the transmission of the necessary funds to London on favourable terms, we think that in some circumstances the Government might fairly consider whether some portion of the funds, which must ultimately be so transmitted, might not, without loss or inconvenience, be retained for a time in India.

160. We fully admit that at this point various considerations come into play. There is the question for instance to which we have already referred of the rate of exchange, and of the possibility that, if full use is not made of the earliest opportunities for remittance, difficulty may be subsequently experienced in transferring to London the money ultimately required there. It must further be remembered that the undertaking of the Secretary of State to sell Council bills without limit at 1*s*. 4$\frac{1}{8}$*d*. per rupee is of material importance in this connection. Then again there is the question of the comparison between the rates of interest obtainable in England and in India respectively, and of the amount which can be safely placed in the one country or the other.

161. But it does not seem to us that the various factors which have to be considered have in the past been fairly set against one another. Indeed a division of business between the Home and Indian authorities has been adopted which seems to us anomalous. The management of the balances in India, it is said, rests with the Government of India. On the other hand, the administration of Council drafts is recognised to rest with the Secretary of State. But it does not seem to have been clearly grasped that the two are interdependent. We have been told that the policy adopted with respect to Council drafts has in fact been to sell freely so long as there was a demand and so long as there were balances sufficient to meet them. In other words, it has been assumed that the proper place for any surplus balances is London. In the great majority of cases this may have been true, but no such general assumption can properly be made when the circumstances are constantly varying. The location of any surplus balances should be determined on a consideration of all the factors. It should be determined further in consultation between the Home and the Indian authorities, and the possibility of the grant of loans to the Indian market should always be considered.

162. The bulk of the evidence offered to us on the subject of these loans has been directed to such questions as, to what auhtorities should advances be made, what amounts ought to be granted or

will be sufficient to prevent stringency and on what terms should they be allowed. With these questions we can deal quite briefly.

163. We think that in the first instance at any rate loans should be confined to the Presidency banks. As occupying a special place in relation to the Government, they are the natural recipients of such loans, and we have no doubt that through them any benefit in easier rates that may accrue will find its way to the other users of money. We observe that the representatives of the Exchange banks agree with this view. All such loans should be secured by the deposit of securities of the Government of India or Port Trust Stocks or similar securities.

164. As regards terms it is clear that, if the objects which we have in view are to be achieved, the present conditions cannot be maintained. In the great majority of cases loans will be possible only when there is a strong demand for money, but we see no reason why the discretion of Government should be limited and loans allowed only in periods of stringency. In any case it seems undesirable to fetter the discretion of Government by making it a condition that no loans are to be granted until the bank rate has reached a particular point. Our attitude is much the same to the proposals frequently made, that loans when granted should be at a prescribed level, whether 1 per cent. or 2 per cent. below bank rate. We think the Government should enter into negotiations with the Presidency banks and lend to them if the terms offered are satisfactory.

165. The question how much may be needed to relieve stringency can only be solved by experience. The amount of the loans will be in any case what the Government, with due regard to all the circumstances of the time, can afford to make and the market can utilise. We do not conceal from ourselves that our general recommendations on this subject involve a considerable departure from previous practice, and may have far-reaching consequences. We advise therefore that in carrying out our proposals the Government should proceed with caution. It is desirable that the change from the old to the new should be gradual and that its effects should be carefully watched. The first steps must be tentative, and in the early stages the Government of India should keep their advances within easily manageable limits.

166. The ultimate effect of these loans upon the Indian money market will be somewhat similar to that which is produced in the United Kingdom by the system of temporary borrowings by Government during the summer and autumn, which are repaid to the market when revenue comes in during the winter. But there is an important difference between Indian and British conditions in this respect owing to the fact that the Government of India are constant borrowers, both in London and in India, for permanent capital expenditure on the development of India's natural resources. The Indian Government regularly go into the money market in India during the summer for a loan in the form of rupee paper. In accordance with the recommendation of the Committee of 1898

(para. 70), that the Indian Government should restrict the growth of their gold obligations, and in view of the well-known advantages of internal over external debt, it has been the recognised policy of the Government to raise in India as large a part as possible of the sums which they require to borrow each year.

167. We have had some evidence, however, to the effect that of recent years the Government's estimates of the amount that could be raised by loans in India have been unduly cautious. The late Finance Member of the Viceroy's Council himself stated in evidence that he had deliberately pursued a cautious policy in this matter. We think that the criticism that undue caution has been used is justified, though the amount involved may not have been very large. It is supported by the facts that at the moment the Government pay less for their borrowings in India than for what they raise in London, and that besides taking up the new issues of rupee paper India has in the last ten years been buying some of the holdings of this security in the United Kingdom.

168. In any case those who are qualified to speak on behalf of the Indian banking community are all agreed in stating that larger loans could be issued each summer in India, if some means were available for counteracting the stringency that recurs annually in the winter and early spring. The practice of making loans from the Paper Currency Reserve and from balances will certainly assist the Government in increasing their annual rupee loans in the summer. The banks would probably be glad to keep larger holdings of Government stocks, if by so doing they did not run the risk of having insufficient liquid resources in the busy season. For the last two years the rupee loan issued in India has amounted to three crores or 2,000,000*l.* If the Government could count on raising larger sums each summer in permanent loans it should be possible for them to reduce to an equivalent extent their estimate of 12,000,000*l.* as the amount of the closing balance required on the 31st March to tide over their summer and autumn requirements. As their capital outlay occurs mainly in the United Kingdom, they will thus be able to release, in payment for Council drafts, some part of the amounts now locked up in the Reserve Treasuries during the busy season.

169. We call attention at this point to the evidence given by some witnesses to the effect that the requirements of the Government of India as regards the endorsements upon the rupee paper and the general form of this security militate against its popularity, particularly among small investors in India. Any reforms which will induce Indians to invest their savings rather than hoard them in metallic form are greatly to be encouraged. We therefore recommend to the attention of the Government of India the questions of the desirability of some relaxation of the present regulations in regard to rupee paper and of creating new forms of securities, such as Treasury bills, short term bonds, or stock redeemable within a moderate period, likely to be taken up by persons to whom rupee paper does not appeal.

(4) Sales of Council Drafts.

(a) *History*.

170. It will be convenient, before turning to the examination of the India Office balance in London, to consider the method of effecting remittances on Government account between India and London, *viz.*, the system of sales of Council drafts. For convenience we use the word drafts to cover both bills and telegraphic transfers.

Sales of Council bills and telegraphic transfers on India by the Secretary of State in London are the central feature of the machinery by which the Indian finance and currency system is at present managed, and a correct understanding of the nature and objects of these sales is the key to the whole system. We have already had occasion to refer to these sales and their uses in several connections; we propose now to consider the system in detail.

171. The practice of drawing funds from India to meet the home charges by means of bills of exchange on India was inherited by the India Office from the East India Company. The present procedure is as follows:—On each Wednesday a notice is exhibited at the Bank of England inviting tenders, to be submitted on the following Wednesday, for bills of exchange and telegraphic transfers on the Indian Government authorities at Calcutta, Madras, and Bombay. The notice states a limit which the aggregate amounts will not exceed. The Secretary of State does not bind himself to allot the whole amount mentioned in the notice, and as a matter of practice does not accept any applications at prices lower than 1*s*. $3\frac{29}{32}$*d*. per rupee for bills and 1*s*. $3\frac{15}{16}$*d*. for transfers. The price charged for telegraphic transfers is ordinarily higher by $\frac{1}{32}$*d*. per rupee than that charged for bills, but when the Calcutta or Bombay Bank rate exceeds eight per cent. tenders for transfers rank for allotment with tenders for bills only if they are $\frac{1}{16}$*d*. higher. Allotment is made to the highest bidders and when the total amount tendered exceeds the amount offered allotment is made *pro rata*. When the tenders received on a Wednesday have been dealt with, the amount to be offered for tender on the following Wednesday is decided upon, the main considerations being the requirements of the India Office and the strength of the demand. "Intermediate" or "special" bills and transfers can be obtained on other days of the week at a price fixed by the India Office at not less than $\frac{1}{32}$*d*. higher than the lowest prices at which allotments have been made on the preceding Wednesday, the exact rate and the maximum amount of such "intermediates" being fixed for the week each Wednesday.

The arrangements made each Wednesday are laid before the next meeting of the Finance Committee of Council, usually on the same day, and subsequently before Council itself, for approval.

172. Up to the time of the closing of the mints to silver in 1893 this weekly auction of Council drafts was nothing more than a simple and effective means of laying down in London the funds re-

quired by the Secretary of State for home charges at as favourable a rate as possible. In times of active trade the Secretary of State sometimes took advantage of a favourable rate of exchange to bring over from India rather more than was needed to meet his immediate requirements, to the mutual advantage ot the Indian revenues and of trade. But the system existed simply as a means of remitting to London so much of the Government balances as it was desirable to make available in London. Its main justification lay in the fact that it was both effective and profitable to the Indian Government and convenient to trade in providing a ready means of settling a large part of the debts due by people in this country (and elsewhere) to people in India for the surplus of exports over imports. Indeed it may be said that it is the large surplus of net exports over net imports which characterises Indian trade in all but abnormal times that makes the system of sales of Council drafts both possible and profitable.

173. With the closing of the mints to silver in 1893, the system of sales of Council drafts assumed new importance, and has been gradually extended in more than one direction. It was by a temporary cessation of the sale of Council drafts that the authorities first tried to force the exchange value of the rupee up to 1*s*. 4*d*. Then, when the rupee finally reached 1*s*. 4*d*. in 1898, under the Act No. II. of 1898 already referred to Council drafts were sold against gold set aside at the Bank of England as a part of the Indian Paper Currency Reserve, and paid for in India out of notes issued against such gold. The object of this action was no longer simply to lay down funds in London for the Secretary of State's home charges, but so to alter the location and disposition of the general resources of the Government of India as to provide a means in a time of great stringency, with the Calcutta and Bombay bank rates standing at 11 and 12 per cent., for quickly expanding the currency as an alternative to the shipment of sovereigns to India on private account when the Government of India had no surplus Treasury balances with which to meet Council drafts.

174. With the development of the Indian currency system on existing lines, and the continued demand for rupees rather than sovereigns for circulation, this new departure of 1898 was developed, and Council drafts came to be used as a means of avoiding the useless accumulation of sovereigns in the Paper Currency Reserve in India. Government had undertaken the obligation of providing rupees in India in exchange for sovereigns at the rate of 1*s*. 4*d*. per rupee. Instead of waiting for the sovereigns to be tendered in India, and accumulate there till they had to be shipped home at Government's expense to purchase silver for coinage into rupees, the Government, as already explained, found it profitable to offer to sell Council bills without limit of amount at 1*s*. 4$\frac{1}{8}$*d*. per rupee, thus receiving payment for the rupees in London instead of in India at a rate of exchange which corresponds roughly with the fixed value of 1*s*. 4*d*. for rupees in India. The money so received in London is either earmarked as a portion of the Paper Currency

Reserve at the Bank of England or used to purchase silver with which to coin rupees to take the place in India of those issued to pay for the Council drafts. A similar train of events has resulted in the issue by the Secretary of State, as occasion requires, of notifications offering to purchase sovereigns in transit from Australia or Egypt to India.

175. Finally in 1909 and 1910, when the exchange crisis of 1907-8 was over, Council drafts were sold freely in order to obtain sterling in London in place of the large quantities of rupees which had accumulated in the Gold Standard Reserve in India through the sale by the Indian Government of bills on London during the crisis, these Council drafts being sold not to provide funds for home charges, but to bring back to London the Gold Standard Reserve fund; and it is by means of sales of Council drafts that the profits on the mintage of rupees, which necessarily first take the form of rupees, are converted into sterling in London, the rupees which represent the profits being issued in India to meet the Council drafts sold in London.

176. It will be seen that the considerations affecting Council drafts are now very much wider than the mere question of laying down in London the funds required for ordinary home charges. The transfer to London from the Government of India's balances of some 20,000,000*l.* annually for the home charges on revenue account and of some 6,000,000*l.* or more to meet capital expenditure remains the chief function of the sales of Council drafts; but if the expense and waste involved in the shipment of sovereigns from India to London on Government account is to be avoided, it is necessary for the Secretary of State to sell sufficient drafts, not merely to meet his own requirements on revenue and capital account, but also to satisfy the demands of trade up to such an amount as will enable the balance of trade in India's favour over and above the amount of the home charges on revenue and capital account to be settled without the export to India on private account of more gold than is actually required in India for absorption by the public.

(*b*) *Management.*

177. The system of Council Drafts has frequently been described as artificial, but within limits, which we shall indicate, it is perfectly natural and would apply whatever might be the currency system in force. The criticism, in fact, that the system is artificial arises chiefly, we imagine, from the fact that the exchange is transacted by the Government themselves, *coram publico*, and little would be heard of it if the Secretary of State's remittances were made through a bank.

178. On the general description of the system which we have given, there cannot, we think, be much disagreement. But differences of opinion at once appear when an attempt is made to define the limits within which its operation is justifiable. The procedure actually adopted, we have been told, in recent years has been to sell

Council Drafts freely, that is to say, to sell as long as there was a demand and as long as it could be met from the resources of Government in India. This statement of the case, however, does not appear to enunciate clearly any principle, and if it is desired to lay down a rule for future guidance we must inquire what is really involved in it. The procedure indicated would seem to be based on one of two alternatives. It may be held, in the first place, that the proper location of the surplus balances of Government is in London, and that as soon as they accrue they should be remitted from India. With this aspect of the case we have dealt already. Or it may be said that it was necessary for Government to supply up to the limit of their power the demand of trade for funds in India, and this position has been taken by some of the witnesses in explanation of the large sales of Council Drafts in recent years. We have already said that we do not favour the view thus implied. The interests of trade are, indeed, of high importance, but it is not the business of Government to favour trade at the expense of general revenues.

179. On the other hand, we have been asked to consider various limitations on the amount of Council Drafts to be sold. Thus it has been suggested that the Secretary of State should never sell more than the amount of his home charges, or that he should restrict his sales to the amount entered in the budget estimates, or again, that he should adjust the sales in such a manner as always to keep his home balance from rising much above the working figure of 4,000,000*l.* To limitations of this kind also we are opposed. The right view is that the extent of the sale of Council Drafts depends on the requirements of Government, whether immediate or prospective, for funds in England. It is true that this principle leaves the Government a wide discretion, and that they may not always exercise it wisely. Their action might then be criticised on the ground that they had brought funds to London prematurely: but this is beside the present point. The fact remains that, while in consequence of recurring surpluses over budget estimates, the London balance has been abnormally high for the last few years, no money has been brought home which has not been used or will not be used for Indian Government requirements in the United Kingdom.

180. On one hand, therefore, the interests of trade are in themselves no justification for sales of Council Drafts in excess of requirements as we have defined them; for if, to accommodate trade, the Secretary of State were actually to go beyond his own needs, it would mean that he would bring to London money for which he had no need and that sooner or later he would have to send it back to India. On the other hand, the attempt to limit sales in advance to any particular sum is arbitrary and unnecessary. The suggestions which we have received in this connection are based on the assumption that Government ought never to bring home more than their immediate requirements, but any such limitation of the discretion of Government would merely interfere with the economical

management of their remittance business without securing any other advantage. Suggestions of this kind seems to be inspired by the feeling that the present system is artificial or that undue assistance is given to trade when sales are less restricted. So long, however, as the Government do not exceed their requirements these fears are groundless. If the Government were to exceed their requirements, they would lay themselves open to the charge of manipulating Government funds for the benefit of trade. Within the limits of those requirements the advantage given to trade is in no sense artificial: there is a corresponding advantage on the Government side, and both arise from that interchange of obligations and resources which forms the general basis of the Council Draft system.

181. From the general limits within which the system is sound we pass to a consideration of the rates at which Council Drafts should be sold. As things are at present, the India Office make a practice of selling Drafts on every Wednesday throughout the year so long as the rate for bills is not below 1*s.* $3\frac{29}{32}$*d.* This is done even if the India Office balance is high enough to dispense with this source of supply for the time being. Several witnesses have criticised this practice, and its justification is not very clear when there is no particular need at the moment for the proceeds of such sales. It is argued in favour of the practice that in this way the India Office are able to feel the pulse of the market and take advantage at once of any increase in demand. But this object could be attained by continuing the invitation for tenders weekly while refusing to sell at very low rates except when money is actually required.

182. Some witnesses, however, went further and urged that the Secretary of State should always sell at a fixed rate, say 1*s.* $4\frac{1}{16}$*d.*, or that he should never sell below par. We are opposed to these suggestions. With regard to the first proposal, we would observe that while the Government are very large dealers in the exchange market, they are not monopolists; and it seems doubtful if they could successfully stand out for any such rate at all times of the year. The increased uncertainty as to the regularity of sales which this policy involves would make it necessary to hold larger normal balances in London than would be otherwise required. The effect of the second proposal, whatever might be the lower rate adopted, would be to limit the range of variation of exchange. With the general object of this proposal we have some sympathy, since the range at present is extensive, and must discourage the free movement of capital between India and other countries. Nevertheless that range, depending as it does on the cost of freight and insurance to India, is the natural range, and any restriction of it would impose additional responsibilities on the Government, for which we find no adequate justification. We consider, therefore, that the Government should continue to follow the market rate, effecting their remittances whenever they find it profitable to do so. In other words, the propriety of the transactions of Government in the exchange market must be judged with reference to the urgency of their requirements and the rate obtainable.

183. In what we have said so far we have had in mind primarily the remittance of Treasury balances, but the same considerations apply also to Council Drafts sold for the purposes of the Paper Currency or Gold Standard Reserves. It has been stated that the system of selling Council Drafts to be met from the Paper Currency Reserve in India originated in the desire to assist trade when Government were unable to meet demands for remittance from their treasury, but it will be clear from what we have said that we do not regard this as a sufficient reason. The justification for such sales must be that, whether for the purchase of silver or for some other purpose, it is considered desirable to hold part of the Paper Currency Reserve in London. Similarly, in the case of the Gold Standard Reserve the sale of Council Drafts is proper in circumstances in which funds belonging to that Reserve have to be transferred to London. In either case the real grounds for remittance must be the home requirements of the Government.

184. We hold, therefore, that, even in the case of the Paper Currency and Gold Standard Reserves, the Secretary of State must have discretion to draw within the limits of what are termed the gold points at the rates obtainable when the remittance becomes necessary. An instructive example of the need of such discretion is supplied by the experience of 1909, when, after the crisis of the preceding two years, a large amount belonging to the Gold Standard Reserve had accumulated in India and was remitted home at a rate considerably below the par of exchange. It has been urged that it would be better when funds belonging to the Gold Standard Reserve are concerned to defer remittance till a rate above par can be obtained. But the first necessity at such a time may be to get the funds to London as soon as possible, in order that they may be available for use in case of any further disturbance of exchange, and we should be unwilling to limit the discretion of the Secretary of State in such circumstances.

185. The opinion is often expressed that, while ordinarily the question of rates may be treated on the lines which we favour, further considerations arise when the sales involve new coinage; and it is suggested that Council Bills should not then be sold below 1*s.* $4\frac{1}{8}$*d.* The suggestion, however, seems to draw too sharp a distinction between the various funds of Government and the purposes to which they are applied. It is always possible, for instance, that the silver required for coinage may be purchased from Treasury funds at home, a transfer being made from the Paper Currency Reserve to the Treasury in India when this silver is shipped and becomes part of the Paper Currency Reserve, and Council Drafts in that case would have to be paid for sooner or later out of the Treasury to make good the home expenditure. Moreover, the suggestion has in view only the gold point as between India and England, whereas rupees may have to be given in exchange for gold imported at various rates from Egypt and Australia and elsewhere. Since further coinage becomes necessary only in times of active trade, exchange naturally tends to be high when fresh coinage is

required. It is desirable that sales for the purpose of new coinage should be kept as closely as possible to specie point (whatever that point may be at the moment): but we think it undesirable to limit the Secretary of State's discretion by rigid rules.

186. We sum up our views as follows:—We cannot agree that the India Office should make a point of not selling drafts in any circumstances below gold export point or below any arbitrarily fixed rate. The general policy pursued at present is, in our view, the right one, *viz.*, to regulate the time and amount of the sales of Council drafts throughout the year according to requirements, so as to take full advantage of the demand for such drafts in order to lay down funds in London. Though the convenience of trade and the regulation of exchange are important considerations for the India Office in the management of the system, we think that in some of the explanations of it given to the public, too much stress has been laid upon this aspect and too little attention has been directed to the primary and by far the most important function of Council drafts, *viz.*, the transfer to London from India of public funds to meet the requirements of the Secretary of State in London. This is true not only of those Council drafts which are met from Treasury balances in India, and serve simply to transfer part of the cash balance from India to London, but also of those which are met from the Reserves in India, since the object of the sales of these drafts is to lay down in London such portions of the two Reserves as the Secretary of State and the Government of India desire to locate in London, either permanently as in the case of the Gold Standard Reserve or the gold portion of the Paper Currency Reserve earmarked at the Bank of England, or temporarily as in the case of moneys belonging to the Paper Currency Reserve which are transferred to London for the purchase of silver for coinage. This is one of the points in which it is particularly important not to overlook the fact that the various funds concerned are, as we have said, really one single whole. If a broad view of the situation is taken, it can be said without departing from accuracy that Council drafts are sold for no other reason and to no larger amount than is necessary to meet the requirements, present or prospective, of the Secretary of State in London.

(5) India Office Balance.

187. We now turn to the examination of the London balance. The primary purpose of the India Office's balance in London is to provide ways and means for meeting the expenditure incurred in the United Kingdom by the Secretary of State on behalf of the Government of India. This expenditure now amounts to something over 20,000,000*l*. a year on revenue account alone, *i.e.*, on salaries, pensions, stores of all kinds, and interest and management of debt and as the amount of Indian debt outstanding in this country tends to grow, this figure is at present increasing slowly year by year. In addition very large sums, estimated in 1913-4 at close on 9,000,000*l*., are required for capital expenditure in London in con-

nection with railways, irrigation works, etc., in India; and the repayment of temporary debt and the guaranteed debentures and bonds of Indian railway companies, whether the money for such repayment is found by fresh borrowing or not, makes considerable calls on the London balance.

188. This balance is fed mainly from two sources, the proceeds of the weekly sales of Council drafts and loans raised in London. There are certain direct sources of revenue which are of little importance, and a variant of the second source is found in the payments made into the balance by Indian railway companies out of the proceeds of the issue of guaranteed stock or bonds issued by or on behalf of those railways, the Indian system being that the Government are shareholders in most of the railways, and act as their bankers both in London and in India. The Secretary of State has a very considerable amount of control over the time and amount of such issues, which may accordingly be regarded for our present purpose as being in the same category with Indian Government loans raised in London.

189. As already stated, the normal balance required on the 31st March in each year in London is about 4,000,000*l*., more than half of this being needed to meet the necessary payments for interest on debt at the beginning of April. When the annual budget is drawn up the Government of India make an estimate of the amount of Council drafts that they will be able to meet from time to time throughout the year. The India Office on the basis of this estimate frame a ways and means budget for the home charges, and arrange to borrow in some form or other the amount required to balance their account. They usually frame their budget, unless for special reasons, so as to estimate for a closing balance at the end of the year of about 4,000,000*l*. If the actual closing balance of the year which is ending is likely to be very much in excess of 4,000,000*l*. they reduce their estimate of borrowings or increase their estimate of capital expenditure for the new year, so as to bring the closing balance of the latter year down to about the normal figure.

190. As the demand for remittance to India is active mainly in the Indian busy season, the greater part of the receipts from Council drafts can only be expected to accrue towards the end of the financial year. The borrowing contemplated in the budget therefore necessarily takes place before it is known how closely the actual receipts will agree with the estimates. Moreover, it is generally recognised that the London money market is more favourable to borrowers in the first half of the calendar year. The India Office accordingly borrow the amount budgetted for either in the first months of the financial year, or sometimes, when market conditions are favourable, as early as February or March in advance of the new financial year. Under existing conditions, therefore, it is impossible for the India Office to regulate their borrowings for the needs of the year in accordance with the surplus or deficit over estimate of their receipts from Council drafts. If, as has happened

recently these receipts exceed the estimate by 10,000,000*l*. or more, the necessary result is that the closing balance of the year largely exceeds the normal 4,000,000*l*. These excess receipts have been due entirely to the recurrence of revenue surpluses in India and their transference to London, with both of which topics we have already dealt. We need only observe, therefore, in regard to the recent accumulation of high balances in London, that a change in the date of the commencement of the financial year, such as we have suggested, would have the further advantage of enabling the India Office to fix the time and amount of their borrowings in London with a more accurate knowledge of their real requirements.

191. Some criticism has been directed against the India Office for not using a larger part of these balances for the discharge of debt. India being a constant borrower for reproductive capital expenditure, the policy of the Government has been, in our opinion rightly, to use their surpluses not in repayment of permanent debt but in the reduction or avoidance of fresh borrowing. We do not agree with those critics who would have advocated the repayment of permanent debt out of the large balances in the years 1910 to 1912, with the result that fresh borrowing would have been requisite soon after. As we have already explained, the continuance of such high balances was not foreseen by the India Office, which necessarily relied on the accuracy of the Government of India's forecasts.

192. But we are inclined to think that in their dealings with the temporary debt the India Office, like the Government of India, are open to the charge of being over-cautious. We would instance in particular the renewal of 1,500,000*l*. of India bills in December 1910 and again in December 1911. The fact that the summer monsoon was over and the probability of some considerable surplus in the receipts from sales of Council drafts could be foreseen by that period of the year would have justified, we think, a less cautious procedure. Another particular instance of what appears to us to have been excessive caution is the flotation of a loan for 3,000,000*l*. in London in April 1912 when the market conditions were very unfavourable, regard being had to the size of the closing balance on 31st March 1912, *viz.*, 18,390,013*l*.; and in looking into this transaction we have found some reason to doubt whether there is sufficiently close consultation between London and India as to the time and amount of particular borrowing operations. It is probable that in 1912 a larger amount than three crores might advantageously have been raised by a rupee loan in July and a smaller amount than 3,000,000*l*. by a sterling loan in London in April.

(6) Lending out of India Office Balance in London.

193. It remains to consider certain special features in the location and management of the India Office balance in London. Under an old-standing arrangement the India Office maintain a minimum balance of 500,000*l*. with the Bank of England with which under the Acts 21 and 22 Vict. c. 106, and 22 and 23 Vict. c.

41, the account of the Secretary of State in the United Kingdom is kept. A very small amount of cash is kept in the till of the Accountant-General at the India Office for daily needs, and some comparatively small amounts are generally held by sub-accountants of the India Office. The rest of the London balance is placed on temporary loan in the City of London.

194. The system of so placing the London balance dates from the time of the East India Company, and is thus an old-established one. A list is kept at the India Office of "Approved Borrowers," admission to which is obtained by application to the Secretary of State's broker, who communicates the application to the India Office. It has always been recognised as the special function of the chairman of the Finance Committee of Council to advise upon such applications. These applications must be considered by the Finance Committee as a whole, but are now submitted after confirmation by that body, for the approval of the Secretary of State in Council. Questions as to the retention of a name on the list are similarly decided. Only firms or individuals of high standing are admitted, and a fixed maximum is laid down in each case for the amounts that may be lent to each borrower. Loans are made in sums of 50,000*l*. or multiples of 50,000*l*. Borrowers are required to deposit at the Bank of England securities of specified kinds against the loans made to them, these securities being transferred into the name or possession of the Secretary of State at the Bank before the loan is made. The full list of approved borrowers as at the 31st March 1913 will be found in Appendix XI.

195. The actual business of finding borrowers is done by the Secretary of State's broker acting under the general directions of the chairman of the Finance Committee. His duty is to place the money at his disposal at the best rate of interest which he can obtain, subject to the general rules already indicated as to the approval of the borrowers and the securities deposited. The appointment of the broker rests with the Secretary of State. The present broker, whose family has long been connected with this particular business, was appointed in 1903 on condition of his becoming a partner in an old-established firm of money-brokers; the appointment was at first for a term of two years, but was renewed in due course, and is now held at the Secretary of State's pleasure.

196. We are satisfied that the system is on the whole well managed, and we have had it in evidence that only in two cases in the last 20 years have borrowers been unable or unwilling to repay their loans on the dates on which they were due, and that in both these cases the Indian Exchequer suffered no ultimate loss. We are, however, of opinion that the facilities for obtaining loans and the method of obtaining admission to the list of approved borrowers might with advantage be made more widely known in the City. And we think that some change is needed in the regulations governing both the kind of securities which are accepted and the amount of cover, if any, required for each of the several classes into which the specified securities are divided.

197. The classification (as revised and extended in February and April 1913) is as follows (*see* Appendix XI., pp. 310 and 312 to 314):—

SECURITIES AUTHORISED FOR ACCEPTANCE.

India Debentures, India Bonds, and Guaranteed Debentures of the several Indian Railway Companies, are taken at their par value.

Treasury Bills, Exchequer Bills, Exchequer Bonds, India Sterling Bills, Metropolitan Water Board Bills, and London County Bills are accepted at their market value, instead of their nominal amount.

The following securities are accepted at their minimum market value, with a cover of 5 per cent., the cover being replaced if the value of the security falls during the currency of the loan:—

Any of the Parliamentary Stocks or Annuities of the United Kingdom.

India $3\frac{1}{2}$ per cent., 3 per cent., or $2\frac{1}{2}$ per cent. Stock, and Stock Certificates.

India Enfaced Rupee Paper.

Fully-paid Debenture Scrip of the Indian Guaranteed Railway Companies.

Any securities, the interest on which is, or shall be, guaranteed by Parliament.

Metropolitan Consolidated Stocks and Stock Certificates.

Metropolitan Police 3 per cent. Debenture Stock.

Metropolitan Water Board "B" Stock, and Stock Certificates.

London County Consolidated Stocks, Stock Certificates and Scrip.

Corporation of London Debentures.

Bonds or Bills of Colonial Governments that have observed the conditions prescribed in the Colonial Stock Act, 1900, 63 and 64 Vict. c. 62, and of British Municipalities with a population of 500,000 or upwards (at present Birmingham, Liverpool, Manchester, and Glasgow), provided that in each case there is an obligation to repay the principal of the bond or bill within a period not exceeding five years from the date on which the loan is granted.

198. We think that the practice of lending upon India Debentures, India Bonds, and Guaranteed Debentures of Indian Railway Compaines at their par value, although the market value may be under par, is unsound. We observe that in the two cases in which borrowers were unable to meet their loans when they fell due the securities deposited consisted of railway debentures of this kind. It was argued by the India Office witnesses in favour of the practice that it enables the Indian Government to make their issues of new

sterling capital on more favourable terms than would otherwise be the case. We are unable to attach much importance to this contention, and in any case we hold that the result obtained does not counterbalance the obvious objections to the course pursued.

199. On the other hand, we are of opinion that the list of approved securities is unduly narrow. We understand that the India Office consider themselves precluded from accepting as security for loans securities transferable elsewhere than at the Bank of England. We think this is unfortunate. We should like to see the list enlarged to cover similar securities registered elsewhere, and it is a matter for consideration whether in addition some of the best Trustee stocks not now in the list might not be accepted to a limited extent subject to the provision of ample cover. In any case it would seem that the narrow boundaries of the existing list needlessly increased the difficulties of the India Office in finding borrowers for the whole of the large balances held during 1910 and the following years, and though we do not feel competent ourselves to draw up a complete list and set of rules, we desire to draw the attention of the Secretary of State to the evidence we have received on the subject and to the considerations set out above.

200. The usual periods for loans to approved borrowers are from three to five weeks, or occasionally six weeks, according to the calculations of the Accountant-General as to the term within those limits for which the money can conveniently be spared. In practice, when large sums are available for lending, the same borrower keeps loans continuously for very much longer periods, through their renewal from time to time after the expiration of the first term. But the prevailing rate of interest has to be paid at each occasion of renewal, and there is no hesitation in requiring repayment if a borrower is unwilling to pay the rate demanded. The criticism has been made that by leaving loans with the same borrower for long periods the India Office have in effect been lending for a long time at rates appropriate only to short-term loans. It would certainly seem that the limit of six weeks is adhered to a little too rigidly, and that some unnecessary caution is exercised in this matter. For instance, no allowance is made, in fixing the dates on which loans are to be repayable, for the receipts likely to accrue from the sale of Council drafts during the interval. We recommend that the present rules should be relaxed whenever a favourable opportunity for lending for any longer period up to (say) three months coincides with ability to spare the money for so long. But it is important that the money should in all circumstances be kept readily available, since it represents a cash balance which should not be diverted from its primary functions for the sake of earning slightly higher rates of interest.

201. We have already alluded to the difficulties which were met with in placing out with approved borrowers the whole of the large balance held by the India Office in London in the years prior to 1913. It is stated that the broker finds himself unable as a rule to place more than from 10,000,000*l*. to 11,000,000*l*. with borrow-

ers on the list under the rules to which he is required to conform. From June 1909 to December 1912 the total India Office balance was considerably higher than 11,000,000*l*. The broker was accordingly directed to place the remainder on deposit with certain specified London banks. The deposit was usually for a period of two months, but sums belonging to the Gold Standard Reserve were occasoinally deposited in this way for three months.

202. In view of the fact that two successive chairmen of the Finance Committee and another member of that Committee were also members of the directorates of banks with which such deposits were made at a time when they held their appointments at the India Office, and that unfavourable comment has been publicly made on this association, we have examined very carefully into the circumstances attending the making of these deposits. We find no ground whatever for the suggestion that the connection between members of the Finance Committee and certain of the banks led to any kind of favouritism being shown to those banks. The deposits were never made at anything less than the best rate of interest obtainable at the time they were made. There was no hesitation in removing a deposit from one bank to another if advantage could be secured by so doing. There is, therefore, no ground for criticism of the way in which this duty was discharged. But we think it advisable to call the attention of the Secretary of State to the importance of avoiding as far as possible all occasion for criticism of this nature, though it may be founded on prejudice and ignorance of the facts.

203. We understand that the charges made by the Bank of England for various services as well as the services themselves are at present under consideration and form the subject of correspondence between the Secretary of State and the Bank. We therefore confine ourselves to observing that in our opinion the time has come for a general review of the whole subject of the relations of the Bank of England with the India Office.

204. Owing to the large balances of the last few years, the remuneration of the India Office broker reached an unprecedented figure. The scale on which it was calculated was thereupon revised. We are not convinced that the principle at present followed of paying him in proportion to the amount of money handled and the rate of interest earned is right. It can hardly be said that the call upon his time varies in exact proportion to the amount of money handled, and after all allowance is made for his skill and zeal in seeking the best rate of interest available, the rate actually obtained must depend much more on the conditions of the money market than on his exertions. We suggest that the working of the present arrangement should be watched. If the balances fall very low, or if they again rise very high, it may require reconsideration. If the principle of a sliding scale be maintained, it would probably be desirable to fix a maximum above which and a minimum below which it should not rise or fall.

IV.—FINANCIAL ORGANISATION AND PROCEDURE OF THE INDIA OFFICE.

205. We have already had occasion to mention and comment upon certain details of the financial organisation and procedure of the India Office in connection with the sales of Council drafts and the system of lending out the cash balance of the India Office in London, and at the beginning of our Report we recorded our very high opinion of the way in which the financial work of the Government of India and of the India Office is performed by the permanent officials to whom it is entrusted. We propose in this section of our Report to confine ourselves to a consideration of general principles.

206. The organisation and procedure of the India Office are conditioned by its legal constitution under a Secretary of State and a Council. This system is necessarily somewhat cumbrous in matters of detail, but it appears to work well on the whole, and must be accepted as the basis of any scheme of organisation which we can consider. Our inquiry will therefore be directed first to the machinery used for bringing financial questions before Council, that is, to the constitution of the Finance Committee of Council, and second to that part of the permanent staff of the India Office which deals with finance.

(a) *Finance Committee of Council.*

207. In considering the constitution of the Finance Committee, we have had our attention drawn to the proposals for a reorganisation of the India Council, outlined by the present Secretary of State in a speech made by him in the House of Lords on the 31st July 1913 after this Commission had begun their sittings. The Secretary of State expressly reserved detailed consideration of his scheme so far as finance is concerned pending the report to be made by us on this portion of our terms of reference. The main features of his scheme are a reduction in the numbers of the Council and the abolition or modification of the Committee system, for which would be substituted a system resembling that already adopted in the Viceroy's Council, under which particular members of Council would be closely attached to particular divisions of the India Office. In regard to finance this would mean the supersession, in whole or in part, of the Finance Committee and the appointment of one member of Council as Finance member at the head of the Financial Department.

208. In this proposal, so far as it affects financial matters, we cannot concur. We are of opinion that the financial work of the India Office, which involves many technical and difficult problems requiring for their consideration a combination of Indian experience with an expert acquaintance with the London money market, is of a kind for which the Committee system is specially suitable, and we think that the continuance of the Finance Committee in

some form is most desirable. It has been suggested that it would be possible to provide for the necessary expert knowledge by means of a Committee of which the members need not all be members of Council. But we see very serious difficulties in the way of any such arrangement. It would seriously impair the status of the members themselves and would deprive them of the opportunity which they now enjoy of obtaining that general knowledge of Indian government and Indian affairs without which they would lose much of their usefulness and nearly all their authority. So far, therefore, as financial work is concerned we recommend the continuance of a Finance Committee of Council.

209. The Finance Committee as now constituted consists of five members of Council, two of whom are bankers connected with large banks in the City of London. These two members have no direct Indian experience. The three remaining members have Indian experience and the members of the Committee represent, in addition to Finance, the Army, Public Works, and General Administration. Since 1880, if not longer, it had been, up to the year 1911, the established practice to have always one member, without Indian experience, who was actively engaged in business in the City, and another with experience of non-official finance, commerce, or banking in India. Besides this, until the retirement of Mr. Finlay in 1906, there was, as a rule, at least one member who had held high financial office in or under the Government of India. Of the last four chairmen of the Committee, three have been City men without Indian experience, and the fourth was one who had been appointed as a representative of Indian commerce, but combined with this qualification an expert knowledge of the London money market.

210. The ideal constitution of the Finance Committee would, in our opinion, include three members with financial experience, two representing respectively Indian official finance and non-official Indian commerce and banking, and one representing the London money market. We see no reason why this ideal should not, as a rule, be attainable; but, if it should occasionally be otherwise, we are of opinion that in all circumstances there should be at least one member with Indian financial experience either official or non-official. We think there are advantages in having a man of Indian experience as chairman of the Finance Committee, but in this matter the Secretary of State should have absolute discretion to appoint the person best suited for the post.

211. It appears to us, in connection with this subject, to be a matter for consideration whether the present pay and tenure of a member of Council are sufficient to attract the best class of financial advisers, more especially in the case of those possessing Indian experience. Until the year 1907 the salary was 1,200*l.* and the tenure of office was for ten years. The salary is now 1,000*l.* and the tenure is for seven years. Considering the immense importance to India of securing the best possible advice and assistance in these

financial matters, we cannot help thinking that the advantages now offered may be inadequate. If that be so, they should be increased.

212. We should deprecate any rule which would have the effect of preventing men actively engaged in business in the City from joining the Council. We are aware of the objections which may be raised, and, as a matter of fact, have been raised, to the present practice; but we consider that they are far outweighed by the advantage of having as a financial adviser a man of the highest standing and repute in daily touch with the money market; and we should see with regret any restrictions which would confine the choice of the Secretary of State to "those who," to use a classical phrase, "have retired from business, or those from whom business has retired."

213. We are fully satisfied that both in the past and at the present time the City of London representatives on the Finance Committee have always kept the interests of India clearly in view, and have performed the duties of their office solely with regard to the welfare of India. But recent political and social changes in India have led to an increasingly close scrutiny in India of the Government's financial administration, and have added very greatly to the amount and the importance of the criticisms which are directed in India against that administration. Moreover, these criticisms now find expression in the form of questions in the Legislative Council which have to be answered by the Government representatives. It appears to us to be hardly compatible with the new conditions in India that just at this time an alteration should have been made in the composition of the India Council and the Finance Committee, involving the omission therefrom of any representation of Indian financial experience, whether official or non-official. The result has been to give the representation of London City experience a position of undue prominence in the Finance Committee, which is, in our opinion, undesirable.

214. We understand that one of the principal objects of the proposals for the reorganisation of the India Council is to expedite business. We think that there is room for improvement in this respect in the financial sphere with which alone we are concerned. But we attach importance to the discussion of all large questions of finance in Finance Committee whenever time admits of it; and the powers of the Secretary of State in respect of the despatch of business are such that he can generally secure such discussion without any undue delay. The Secretary of State has already confided large discretionary powers to the chairman, and these will no doubt be continued, and will enable him to act, either alone or with the special sanction of the Secretary of State, whenever prompt measures are necessary. We desire, however, to make it clear that, subject to the conditions which we have laid down in this and the preceding paragraphs, we should welcome any changes, whether requiring legislative sanction or not, which would simplify financial procedure and prevent unnecessary delay in the consideration and determination of questions of a financial character.

(b) *Permanent Staff of the India Office.*

215. At the head of the Financial Department of the India Office, but subordinate to the Permanent Under Secretary of State and to the Assistant Under Secretary, is the Financial Secretary, upon whom fall the main burden and responsibility for the financial work of the office. At the present time it happens that the Assistant Under Secretary of State is an officer trained in the Fnancial Department and equipped with extensive knowledge of finance. He is thus able to offer useful advice to the Financial Secretary in the many cases in which a second opinion is desirable, and considerably to lighten his burden and responsibility. It is also possible to focus · the hands of the Assistant Under Secretary the consideration of financial questions originating in divisions other than the Fnancial Department and submitted to the higher authorities by the heads of those divisions. This arrangement has obvious advantages, and has served to relieve the Financial Secretary, who, until it was adopted, was undeniably overworked.

216. It appears to us that a return to the previous system, which threw the whole burden of supplying special financial knowledge and criticism upon the Financial Secretary, is, if not impossible, certainly undesirable. For the future, it has been suggested either (1) that the Under Secretary of State or the Assistant Under Secretary should have financial experience; or (2) that there should be two Assistant Under Secretaries, of whom one should have had financial training. As between these alternatives we are unwilling to express an opinion, believing that the choice must depend largely upon the varying circumstances of the time and on the material at the disposal of the Secretary of State. We are content to record our opinion that, in one or other of these ways, the burden of work and responsibility which previously fell upon the Financial Secretary should continue to be diminished, as it is under the existing arrangement. It has also been suggested that the Financial Department should be strengthened by the appointment of a second Financial Secretary, to whom business of a technically financial character should be specially allotted. We bring this suggestion to the attention of the Secretary of State.

The pecuniary value to India of the efficient performance of the financial business of the India Office is very great and would amply justify any extra cost in salaries that might arise from the adoption of our recommendations.

V.—STATE OR CENTRAL BANK.

217. We have made no reference to the State Bank question in the earlier passages of our Report, in spite of its frequent relevance, because we were unwilling to introduce, in passing, remarks which might appear to prejudge, one way or the other, a question which we were not prepared to discuss in detail. Many of our recommendations, notably those which relate to the maintenance

of exchange, the position of gold in the currency, the system of budgetting, and the raising of loans by Government, are not appreciably affected by any decision which may be arrived at on the bank question. But others, especially those which relate to the elasticity and fiduciary portion of the note issue, to the custody, employment, and proper amount of the Government balances in India and London, and to remittance, are somewhat intimately bound up with the presence or absence of a State bank. The bank question has also a close connection with subjects not directly falling within the terms of our reference, such as the absence of a final banking reserve in India and the question of giving the Presidency banks access to London, the extension of co-operative credit in India, the improvement of banking facilities and the encouragement of sound banking in that country.

218. It has been represented to us that, under several of these heads, the difficulties and inconveniences which arise are largely contingent on the absence of a strong central banking institution, competent to manage the note issue, and so constituted as to be in a position to hold and manage the whole of the Government balances and to transact for Government other business naturally falling within the province of the Government's banker, such as remittance. In the lack of such an institution the Government of India's position, while not unexampled, is unusual. So long as the Government remain aloof from banking, so long as they maintain (to any important extent) an independent treasury system, and so long as the management of the note issue is kept outside banking, some features of the present system, which may be regarded as anomalous, will remain. We have endeavoured in the preceding parts of our Report to make such recommendations as will permit the continuance of these features with as little general inconvenience as possible. But those which relate to the note issue and to the employment of balances may be regarded, from one point of view, as palliatives rather than cures.

219. We have been naturally led, therefore, to give some consideration to the possibility of such more radical changes as are contingent on the establishment of a State bank—a proposal which presents at the same time some attractive features and some obvious practical difficulties. But we found from the outset in examining witnesses upon the subject of a State or Central Bank that the absence of anything in the nature of concrete proposals and even of any general agreement as to what was implied by the phrase "a State or Central Bank" made such examination difficult and unsatisfactory. It was arranged, therefore, before we adjourned for the summer holiday in August, that two of our number, Sir Ernest Cable and Mr. J. M. Keynes, should prepare a detailed scheme for their colleagues' consideration. We annex to our Report the memorandum submitted to us by Mr. Keynes, after collaboration with Sir Ernest Cable, in accordance with this decision.

220. We had previously received the memorandum on the subject of a State Bank or Central Bank submitted to us by Mr. L.

Abrahams, C.B., with the concurrence of the Secretary of State. This memorandum was printed as Appendix No. XIV. to our Interim Report. The memoranda in question indicate most of the advantages and disadvantages attaching to the proposal on general grounds and the considerations to be borne in mind in dealing with it. It is unnecessary for us to recapitulate them here.

221. A study of these two memoranda makes much clearer the nature of the questions at issue; and the schemes proposed in them present *primâ facie* several attractive features. But most of the witnesses whom we have examined had not been in a position to consider or pronounce upon the specific proposals therein contained. It was not possible for us, therefore, to submit these schemes to a sufficiently searching examination without much delay in the presentation of our Report. We recognised, further, that such an examination would probably involve a visit to India and a careful study of the conditions on the spot, and we came to the conclusion that we were not fitted as a body to undertake this task. We do not feel ourselves, therefore, in a position to make recommendations, one way or the other, on the question of a State Bank.

222. But we regard the question, whatever decision may ultimately be arrived at upon it, as one of great importance to India, which deserves the careful and early consideration of the Secretary of State and the Government of India. We think, therefore, that they would do well to hold an inquiry into it without delay, and to appoint for this purpose a small expert body, representative both of official and non-official experience, with directions to study the whole question in India in consultation with the persons and bodies primarily interested, such as the Presidency banks, and either to pronounce definitely against the desirability of the establishment of a State or Central Bank in India at the present time, or to submit to the authorities a concrete scheme for the establishment of such a bank fully worked out in all its details and capable of immediate application.

VI.—SUMMARY OF CONCLUSIONS.

223. For convenience of reference we summarise our conclusions as follows:—

(i) The establishment of the exchange value of the rupee on a stable basis has been and is of the first importance to India. (Para. 8.)

(ii) The measures adopted for the maintenance of the exchange value of the rupee have been necessarily and rightly rather supplementary to, than in all respects directly in pursuance of, the recommendations of the Committee of 1898. (Paras. 7 and 44 to 46.)

(iii) These measures worked well in the crisis of 1907-8, the only occasion upon which they have been severely tested hitherto. (Paras. 48, 49.)

(iv) The time has now arrived for a reconsideration of the ultimate goal of the Indian Currency system. The belief of the Committee of 1898 was that a Gold Currency in active circulation is an essential condition of the maintenance of the Gold Standard in India, but the history of the last 15 years shows that the Gold Standard has been firmly secured without this condition. (Paras. 47, 50.)

(v) It would not be to India's advantage to encourage an increased use of gold in the internal circulation. (Para. 64.)

(vi) The people of India neither desire nor need any considerable amount of gold for circulation as currency, and the currency most generally suitable for the internal needs of India consists of rupees and notes. (Paras. 55, 76.)

(vii) A mint for the coinage of gold is not needed for purposes of currency or exchange, but if Indian sentiment genuinely demands it and the Government of India are prepared to incur the expense, there is no objection in principle to its establishment either from the Indian or from the Imperial standpoint: provided that the coin minted is the sovereign (or the half-sovereign); and it is pre-eminently a question in which Indian sentiment should prevail. (Paras. 69—73.)

(viii) If a mint for the coinage of gold is not established, refined gold should be received at the Bombay Mint in exchange for currency. (Para. 73.)

(ix) The Government should continue to aim at giving the people the form of currency which they demand, whether rupees, notes, or gold, but the use of notes should be encouraged. (Para. 76.)

(x) The essential point is that this internal currency should be supported for exchange purposes by a thoroughly adequate reserve of gold and sterling. (Para. 76.)

(xi) No limit can at present be fixed to the amount up to which the Gold Standard Reserve should be accumulated. (Para. 86.)

(xii) The profits on coinage of rupees should for the present continue to be credited exclusively to the Reserve. (Para. 89.)

(xiii) A much larger proportion of the Reserve should be held in actual gold. By an exchange of assets between this Reserve and the Paper Currency Reserve, a total of about 10,000,000*l*. in gold can be at once secured. This total should be raised as opportunity offers to 15,000,000*l*., and thereafter the authorities should aim at keeping one-half of the total Reserve in actual gold. (Paras. 93 to 100.)

(xiv) The Indian branch of the Gold Standard Reserve in which rupees are now held should be abolished, the rupees being handed over to the Paper Currency Reserve in exchange for gold. (Para. 98.)

(xv) The proper place for the location of the whole of the Gold Standard Reserve is London. (Paras. 90 and 100.)

(xvi) The Government should definitely undertake to sell bills in India on London at the rate of 1*s*. $3\frac{29}{32}$*d*. per rupee whenever called upon to do so. (Para. 101.)

(xvii) The Paper Currency system of India should be made more elastic. The fiduciary portion of the note issue should be increased at once from 14 crores to 20 crores, and thereafter fixed at a maximum of the amount of notes held by Government in the Reserve Treasuries *plus* one-third of the net circulation, and the Government should take power to make temporary investments or loans from the fiduciary portion within this maximum in India and in London, as an alternative to investment in permanent securities. (Paras. 112 and 113.)

(xviii) We recommend the immediate universalisation of the 500-rupee note and the increase of the facilities for the encashment of notes. (Para. 115.)

(xix) The aggregate balances in India and London in recent years have been unusually large. This has been due mainly, though not entirely, to accidental causes and to the exceptional prosperity of India. (Paras. 125, 126.)

(xx) Caution is justifiable in framing Budgets in India, but has been carried rather further than was necessary in recent years. (Paras. 126 and 128.)

(xxi) A change in the date of the commencement of the financial year from the 1st April to the 1st November or the 1st January would probably enable the Government of India to frame more accurate Budgets. Such a change would also enable the India Office to fix the amount of their borrowings in London with closer regard to immediate needs. We commend this proposal for favourable consideration. (Paras. 128 and 190.)

(xxii) The practice of transferring revenue surpluses to London to be used in avoiding or reducing fresh borrowings for capital expenditure has been thoroughly justified in the interests of India, and the Secretary of State has made good use, for this purpose or for actual reduction of debt, of the balances from time to time accumulated in his hands. (Paras. 130 to 133 and 179.)

(xxiii) But the recommendations which we make as regards loans by Government in India may lead to a revision of

the occasions, though not of the extent, of transfers of money to London. (Para. 133.)

(xxiv) The independent Treasury system of the Indian Government is not an ideal one. It is partly responsible for the stringency which recurs annually in the Indian money markets. (Paras. 137 to 143.)

(xxv) We recommend that the Government of India should make a regular practice of granting loans to the Presidency Banks from their surplus balances in India against security on terms to be negotiated with the Presidency Banks. (Paras. 150, 163, 164.)

(xxvi) In deciding upon the location of surplus balances, the Government of India and the Secretary of State should act in consultation, and, while the transmission of the necessary funds to London at favourable rates of exchange is the first consideration, the authorities should have regard to all the factors including the possibility of utilising surplus balances for loans in India. (Paras. 159 to 161.)

(xxvii) In carrying out these recommendations, the authorities should proceed tentatively and with caution. (Para. 165.)

(xxviii) We recommend that the amount of the annual rupee loans in India should be increased as much as possible. The figures of recent loans appear to have been somewhat over-cautious. We call attention to the questions of relaxing present regulations in regard to endorsements on rupee paper and of creating new forms of securities. (Paras. 167 to 169.)

(xxix) The Secretary of State sells Council Drafts, not for the convenience of trade, but to provide the funds needed in London to meet the requirements of the Secretary of State on India's behalf. (Para. 186.)

(xxx) The India Office perhaps sold Council Drafts unnecessarily at very low rates on occasions when the London balance was in no need of replenishment, but we do not recommend any restrictions upon the absolute discretion of the Secretary of State as to the amount of drafts sold or the rate at which they are sold, provided that it is within the gold points. The amount and occasion of sales should be fixed with reference to the urgency of the Government's requirements and the rate of exchange obtainable, whether the drafts are against Treasury balances or against the Reserves. (Paras. 181 to 185.)

(xxxi) There has been some excess of caution in the renewal of debt by the India Office during recent years. (Para. 192.)

(xxxii) The system of placing portions of the India Office balance out on short loan with approved borrowers in the City of London is on the whole well managed, but we draw attention to—

(*a*) The term for which loans are made.

(*b*) The desirability of giving greater publicity to the methods by which admission is gained to the list of approved borrowers.

(*c*) Some defects in the list of approved securities and especially its narrow range. (Paras. 196 to 200.)

(xxxiii) There is no ground for the suggestion that the City members of the Secretary of State's Council showed any kind of favouritism in placing on deposit with certain banks, with the directorates of which they were connected, a part of the India Office balance at a time when it was too large to be placed entirely with the approved borrowers. But we call the attention of the Secretary of State to the desirability of avoiding as far as possible all occasion for such criticism, though it may be founded on prejudice and ignorance of the facts. (Para. 202.)

(xxxiv) We observe that in our opinion the time has come for a general review of the relations of the India Office to the Bank of England. (Para. 203.)

(xxxv) The working of the present arrangements for the remuneration of the Secretary of State's broker should be watched, and if necessary they should be revised. (Para. 204.)

(xxxvi) We record our high opinion of the way in wihch the permanent staff, both in India and in London, have performed the complicated and difficult financial duties placed upon them. (Para. 7.)

(xxxvii) We recommend a continuance of a Finance Committee of Council as providing the machinery most suitable for the work required. (Para. 208.)

(xxxviii) The Finance Committee should, if possible, contain three members with financial experience, representing—

(*a*) Indian Official Finance.

(*b*) Indian Banking and Commerce.

(*c*) The London Money Market.

In any case there should be at least one member with Indian financial experience. The absence of any representative of Indian finance on the Committee since 1911 has resulted in giving undue prominence to the representation of London City experience. (Para. 210.)

(xxxix) While we suggest that the changes recently proposed and now under discussion in the constitution of the India Council may require some modification in order

to provide for the continuance of a Finance Committee of Council, we are in sympathy with the desire for expediting financial business, which is one of the objects in view. (Para. 214.)

(xl) The present arrangement under which the Assistant Under Secretary of State, having financial experience, is able to share with the Financial Secretary the responsibility for financial business in the India Office has many advantages. For the future we recommend that either (1) the Under Secretary or Assistant Under Secretary of State should have financial experience as at present, or (2) there should be two Assistant Under Secretaries, of whom one should have financial experience. (Para. 216.)

(xli) We are not in a position to report either for or against the establishment of a State or Central Bank, but we regard the subject as one which deserves early and careful consideration, and suggest the appointment of a small expert committee to examine the whole question in India, and either to pronounce against the proposal or to work out in full detail a concrete scheme capable of immediate adoption. (Paras. 221, 222.)

224. We desire to place on record our high appreciation of the valuable assistance which we have received from Mr. Blackett and Mr. Smith in the course of our inquiry. To Mr. Blackett in particular we have entrusted a great deal of extremely important work, and he has discharged the duties imposed upon him with great ability and unfailing courtesy and tact.

AUSTEN CHAMBERLAIN (*Chairman*).
FABER.
KILBRACKEN.
ROBERT CHALMERS.
ERNEST CABLE.
S. B. BROACHA.
J. BEGBIE.*
R. W. GILLAN.
H. N. GLADSTONE.
J. M. KEYNES.

BASIL P. BLACKETT,
Secretary.

Dated the 24th day of February 1914.

*Subject to note on p. 229

ANNEXE TO REPORT OF ROYAL COMMISSION ON INDIAN FINANCE AND CURRENCY.

Memorandum by Mr. J. M. Keynes on proposals for the establishment of a State Bank in India.

CONTENTS.

[This memorandum was drawn up in the summer of 1913 by Mr. J. M. Keynes, in collaboration with Sir Ernest Cable, at the request of their colleagues on the Royal Commission. It retains a form originally designed with a view to the private use of the Commission rather than to publication, and in a few passages where its subject overlaps with that of the Report it shows the influence of some conclusions tentatively reached by the Commission in the summer.]

Memorandum on Proposals for the Establishment of a State Bank in India.

I.

INTRODUCTORY.

A Central Bank must necessarily stand in a somewhat close relation to Government. If the Bank is to be useful, it must have the management of the Government balances and of the note issue. It would be contrary to experience elsewhere and to what seems reasonable for India to hand over these functions to a purely private institution. If Government is to interfere at all, it cannot help involving itself in ultimate responsibility for the Bank, and if it is thus to involve itself, its powers must be sufficient to permit an effective supervision. From a Government with feeble powers and placed in the position of interested but irresponsible critics, there would be a greater likelihood of vexatious interference; while too great a dependence on the terms of the Bank's charter must tend to make these terms rigid and narrow for practice.

The constitutions of the principal State Banks of Europe and of the Bank of Japan are briefly outlined in an appendix to this Memorandum. Their general character points overwhelmingly to the conclusion that the higher executive officers responsible for the policy and administration of the Bank must be appointed by Government and rest under its ultimate authority. In all State Banks of importance the influence of the shareholders is chiefly consultative and advisory.

If these preliminary points are granted, we are at once faced with a somewhat different proposal from that which the Government had before them in 1900—1902. The position at that time seems to have been that, if the Presidency Banks would amalgamate on their own initiative and also increase their capital by a substantial amount, the Government would seriously consider the handing over to them, on terms to be discussed later, of the management of the paper currency and the use of a large portion of the public balances. The advantages to be gained by the Presidency Banks were insufficiently certain or precise, and the proposals fell through. Several of the difficulties which have appeared serious to some of our witnesses are more relevant, I think, to the proposals of 1900—1902 and to the popular idea of a State Bank thus fostered than to the proposals to be developed below.

The question why anyone should wish to set up a State Bank and the advantages to be got from it are treated in section VIII. Section II is devoted solely to the problem whether it is feasible to devise for such a Bank a working constitution.

The main difficulties to be faced are the following:—

(i) To combine ultimate Government responsibility with a high degree of day-to-day independence for the authorities of the Bank.

(ii) To preserve unimpaired authority in the executive officers of the Bank, whose duty it would be to take a broad and not always a purely commercial view of policy, and at the same time to make use of the commercial instincts and commercial knowledge of representatives of the shareholders.

(iii) To maintain in the day-to-day management of the Bank the high degree of decentralisation to which great importance is rightly attached in the case of so large a country as India.*

Further points, such as the *status* of the Bank in London, the method of regulation of the note issue, the division of profits between the shareholders and the Government, no doubt present difficulties. But these must certainly be capable of some solution. Fundamental objections to the proposed Bank must arise out of its failure to satisfy the three main conditions set out above.

An outline constitution so far as affects these three fundamental points is given below.

II.

OUTLINE CONSTITUTION, SO FAR AS CONCERNS THE RELATION OF THE BANK TO GOVERNMENT, THE POWERS OF THE SHAREHOLDERS, AND DECENTRALISATION.

1. The supreme direction of the Imperial Bank of India shall be vested in a Central Board of three members, consisting of the Governor of the Bank (who shall be Chairman), the Deputy Governor, and a representative of Government, together with three or more Assessors.

2. The Governor shall be appointed for periods of 5 years (subject to age limit) by the King on the recommendation of the Secretary of State, and shall be removable in like manner. He shall be eligible for re-appointment. The salary of the Governor shall be Rs. 1,00,000 per annum.†

3. The representative of Government shall be appointed by the Viceroy and shall be, in general, the Financial Member of the

* As the Government of India wrote to the Secretary of State when advocating the establishment of a Central Bank (January 18, 1900):—"Nothing would be more unwise than to discard the valuable local knowledge, skill and experience of the existing directorates and managements of the Presidency Banks."

† These figures are put forward very tentatively, to suggest the status of the officers affected.

Viceroy's Council, the Member for Commerce and Industry, or the Secretary from the Department of one of them.*

4. The Assessors shall be the Managers of the three Presidency Head Offices (*see* below) and of such other Head Offices as may be created hereafter, or their Deputies. The Assessors shall have the right to attend any meeting of the Central Board and to lay their views before it, but shall not vote. The Central Board shall also have the right to summon any of the Assessors to attendance.

5. The Deputy Governor of the Bank, and Managers of the Presidency Head Offices, who shall all be of the same status and receive salaries of Rs. 60,000† shall be appointed by the Viceroy on the nomination of the Governor of the Bank and of the Government representative on the Central Board. But the appointment of a Manager to a Presidency Head Office shall be subject to the approval of the Presidency Board (including representatives of the shareholders) of the Head Office in question.

6. Within the limits of the Bank Act, the Central Board shall have absolute authority, and the signature of the Governor supported by a majority vote of the Board shall be legally binding upon the Bank; save that the representative of the Government shall have discretionary power (for use in emergencies only) to suspend the carrying into effect of any decision until it has been reported to the Viceroy, with whom shall lie an ultimate right of veto.

7. The Central Board, which will have no direct dealings with the public, shall have its offices and establishment located at Delhi (or Calcutta). Its members will keep in touch with the chief commercial centres of the country, partly by the attendance from time to time of the Assessors, and partly by touring on the part of the Governor or his Deputy.

8. All transactions between the Bank and the public in India shall be under the authority of one or other of the Head Offices. In the first instance, Presidency Head Offices shall be established at Calcutta, Bombay and Madras, and the spheres of influence of these Head Offices shall be the same as those of the existing Presidency Banks.‡

9. Each Head Office shall be under the direction of a Presidency Board, consisting of the Manager (who shall be Chairman and have the casting vote), the Deputy Manager, a representative of the Local Government, and three (or four) unofficial members.

10. The unofficial members shall be elected by the shareholders on the local register of each Presidency from amongst their own number.

11. Any business, within the limits of the Bank Act, and not contrary to the express instructions of the Central Board, entered into by a Presidency Board, shall be legally binding on the Bank.

* Or the Comptroller of Currency, the proposed appointment of whom has been lately announced.

† These figures are put forward very tentatively, to suggest the status of the officers affected.

‡ Including Ceylon, as at present in the case of the Madras Head Office.

12. Although the Central Board shall have authority to issue instructions, to which the Presidency Boards shall be subject, on all matters, nevertheless in general, and failing special prior instructions to the contrary, a Presidency Board shall have entire discretion to transact on its own authority all business of the following descriptions:—

(1) To discount Indian (rupee) trade bills, maturing within a maximum period of six months, subject to a minimum rate arranged from time to time in consultation with the Central Board;

(2) To rediscount sterling trade bills, bearing the endorsement of another bank, subject to minimum rate arranged from time to time in consultation with the Central Board, and subject to daily report to the Central Board.

(3) To make interest-bearing loans (subject to a minimum rate, etc.), for periods not exceeding six months against such kind of security as is permitted by the Bank Act.

(4) To buy and sell in India, subject to daily report to the Central Board, gold bullion and such bonds and securities as may be dealt in according to the provisions of the Bank Act.

(5) To provide trade remittance for customers to all parts of India, and private remittance to London subject to certain conditions.

(6) To accept interest and non-interest bearing deposits, subject to a maximum rate, etc.

(7) To accept valuable goods for safe keeping.

(8) To open, staff, and control branch banks at any place within the Presidency Board's sphere of influence.

13. A general report on all such transactions shall be forwarded to the Central Board weekly, and more frequently when the Presidency Board think it desirable, or the Central Board request it.

14. In regard to the rates charged for discounts and loans, and allowed on deposits the Presidency Boards shall be free to vary the rate charged in individual transactions and at their different branches, subject to minimum (or maximum) rates, fixed weekly (or in emergency more frequently) in consultation with the Central Board.

III.

DISCUSSION OF THE OUTLINE CONSTITUTION.

The object of the above draft proposals is merely to indicate in a more precise way than is otherwise possible the kind of relations which are contemplated between the Government, the Central Board, the Presidency Boards, and the shareholders. It will be worth while to discuss these points more fully and to consider also

how far such proposals satisfy the three fundamental conditions which were laid down in I.

1. First, as regards the relation of the Bank to the Government. The creation of such a bank as is here proposed certainly increases in a sense the responsibilities of Government. But there are two senses of the term "responsibility." The Government may be said to be responsible if, in the last resort, it is the Government that has to come to the rescue. Or it may be held that it can only be called responsible if, in addition to this, it is the proper object of criticism or blame if anything goes wrong. Those acquainted with the present banking position in India would maintain, I think, that the Government already possesses responsibility in the first and more important sense. So long as they manage the note issue, and maintain large cash balances outside the ordinary banking system, they are bound to come to the rescue of the Presidency Banks in the event of a widespread crisis involving the banks generally.

The prevention of occurrences contrary to the public interest, rather than the avoidance of responsibility, ought in general to be the first object of Government. The only good reason for avoiding responsibility in the first sense is in the case of kinds of action which Governments are not competent or have not the machinery to perform well; and the only good reason for avoiding it in the second sense, when it already exists in the first, is in cases where explicit responsibility would involve them in such unpopularity or criticism as might impair their general efficiency. It cannot be maintained that some responsibility for banking, seeing that it is in fact undertaken by nearly all civilised Governments, is inherently undesirable. The undesirable features in the Government's present degree of responsibility for these things in India are rather due to the lack of suitable machinery. I need not enlarge on this. There is an absence of trained experience and specialised knowledge on the part of those responsible, so that financial duties are apt to be thrown on officers concerned, during the greater part of their careers, with quite other things. The business is of a kind where immediate action and undivided responsibility in regard to details is essential, whereas, if it is dealt with in the ordinary mills of Government, this is nearly impossible. But given a suitable machinery I do not see why anyone should wish to divest Government of the duties in question. That the solution lies in the provision of a more suitable machinery, rather than in the getting rid of existing functions, has been strongly impressed on me in the course of the Commission's deliberations. This more suitable machinery the creation of a State Bank affords.

It seems clear that Government cannot entrust any of its existing duties to private hands. It has also become plain that, whether a State Bank is established or not, Government, so far from relinquishing old duties, must bend itself to new ones. The functions of the note issue, it is generally agreed, must be extended, and an element of discretion must be introduced where there was previously

none. As in the case of the note issue, so in the case of the cash balances, there must be less rigidity of rule and more discretion. Now, with a State Bank all this would be easy, and there are plenty of precedents to look to; but as soon as an attempt is made to work out precisely by what sort of procedure these objects are to be attained in the absence of a State Bank, it becomes apparent that it is not altogether through chance or obtuseness that such desirable changes have not been made long ago. The existing system has been deeply conditioned by the absence of a State Bank. The history of the management of the cash balances, for example, bears witness to this. At no time has any one supposed the existing system to be perfectly satisfactory. It has established itself because it is the only system which frees the officials from the exercise of a discretion for which they do not feel themselves competent and from which they therefore shrink. The evidence is that actual practice has always tended to be more rigid than the actual letter of the rule laid down by the Secretary of State; and naturally enough. Similarly in regard to the paper currency. In the first instance, no doubt, the system was set up in uncritical imitation of the Bank of England's, and under the influence of the theory that it was a positive advantage for note issue to be separated from banking; but for 30 years at least this theory has lacked vitality or offspring, and note issue in India has remained divorced from banking because there has been no bank to join it to, and because, for a rule-of-thumb system, it is a fairly good one.

The choice lies between a good deal of responsibility *without* thoroughly satisfactory machinery for the discharge of it; and a little more responsibility *with* such a machinery. The balance of advantage is with the second alternative.

As regards the Secretary of State's exposure to pressure or parliamentary criticism of an undesirable kind, the creation of a State Bank would, without question, improve and strengthen his position. Recent experience shows that he cannot, under the present system, resist cross-examination on minute details of financial management. If arrangements are introduced for loans from the cash balances and for some degree of regulation of the currency reserve by discretion, will he not be liable to all kinds of questions in Parliament on details of executive policy? If the Government of India is lending three crores from the cash balances and some business men think they would like four crores, what will there be to prevent the working up of a strong agitation by means of the Press, daily fed and inflamed by questions in the House, for lending on a larger scale? I do not see how the Secretary of State could be more exposed than he is to what may really be a most undesirable thing, namely, cross-examination on actions which are, in truth, none of his business.

The State Bank, on the other hand, would have a high degree of independence; and there would be numerous questions to which the Secretary of State's proper answer would be that it was entirely a matter for the Bank. He would never admit, for example, the

faintest degree of responsibility for the precise level of the bank rate at a particular moment. The Secretary of State would be behind the Bank, but his authority would only come into play on rare and important occasions. On important changes of policy and on alterations of clauses in the Bank Act, the Secretary of State would have the last word and with it the responsibility. If over a period of time there were a widespread feeling that the regular administration of the Bank was ill-conducted, it would be his duty to grant an inquiry and to act in the light of its report. But for the ordinary daily work of the Bank he would necessarily disclaim responsibility to a far completer extent than is at present possible in the case of any of the financial business now conducted by the Government. The method of appointment suggested above of the Governor and Deputy Governor is intended not to make them Government officials, but to place them in a position of considerable independence. A State Bank would certainly act as a buffer of no little importance between the Secretary of State and external pressure of an undesirable kind.

This day-to-day independence of the Bank, which would incidentally prove a relief to the Secretary of State, would be absolutely essential from the Bank's own point of view. It is not likely that the commercial community would acquiesce in any proposal where it was absent. Banking business must be outside the regular Government machine, ignorant of "proper channels," and free of the official hierarchy where action cannot be taken until reference has been made to a higher authority. The officials of the Bank should have precisely the same powers for the prompt transaction of business that the officials of the Presidency Banks have now.

The presence of private capital is probably a considerable bulwark against some kinds of political pressure. Continental experience shows that private ownership of the Bank's capital, even although the shareholders have no more than advisory powers, is an important safeguard of the Bank's independence; and continental writers have laid great stress on this.*

The outline constitution given above has been designed with a view to these conditions. The Bank, though ultimately dependent on the State, would lie altogether outside the ordinary Government machine; and its executive officers would be free, on the one hand, from the administrative interference of Government and free also, on the other hand, from too much pressure on the part of the shareholders, in cases where this might run counter to the general interest.

A State Bank of the kind proposed might really get the best of both worlds. It is difficult to predict how a new institution will work out in practice. But the advantages of a State and of a

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* *See* Appendix B.

private institution may be, partly at any rate, combined. Representatives of the public interest must have the ultimate control, because a State Bank is given powerful monopolistic rights; and the public interest may not invariably be at one with the interests of shareholders, though on the whole and generally speaking the shareholders must benefit largely by their connection with the State. On the other hand the alliance of the State with private shareholders serves to keep the executive of the Bank in close touch with commercial opinion, and introduces that element of commercial self-interest, from which, in the present economic arrangement of affairs, a State Bank, as well as private institutions, may derive a real advantage.*

It may be added in this connection that the Governor and Deputy Governor of the Bank should invariably be persons of commercial or banking, not of administrative or official, experience, and should be appointed, so far as may be possible or convenient from the staffs of the Presidency Offices. Though it would not be wise to lay down any rule or principle on the matter, and while it might be an advantageous thing to introduce from time to time officers whose banking experience had lain elsewhere, the Governorship of the Bank should be a position to which the leading officials of the Presidency Offices could reasonably look forward as a possible prize. It might, perhaps, increase public confidence in the non-official character of the Bank's management and in the Government's intentions, if it were definitely laid down that members of the English or the Indian Civil Service were ineligible for appointment as officers of the Bank.

2. Second as regards the relation of the Central Board to the Presidency Boards, and the arrangements for decentralisation. We are here presented with a problem which is largely peculiar to India. But a little may be learnt from the organisation of the Head Offices of the Reichsbank described in Appendix A; and the establishment of local Committees or Directorates is fairly familiar in the case of many important banks doing business partly in London and partly abroad.

It is clear that the organism of the Central Board must be quite distinct from that of any of the Presidency Head Offices. It would be undesirable, *e.g.*, that the Calcutta Office should be superior in any way to the Bombay Office. The Presidency Boards and Presidency Offices must all be on a complete equality and

* The same point is emphasised in the following quotation from the official history of the Reichsbank:—"Through the co-operation of the Reichsbank authorities, who are not interested in the financial profits of the Bank, with the representatives of the shareholders, who are practical business men, the Bank management is safeguarded, since it takes into consideration the interest of the public; and at the same time the experience and business knowledge of the shareholders, who are financially interested in the success of the Bank, are utilised in the guidance of the Bank. This a purely private one, has proved to be the best system according to the a purely private one, has proved to be the best system according to the experience of most European countries."

stand in the same relation to the Central Board. Even if it proved convenient for the offices of the Central Board to be located in Calcutta, this Board would be quite distinct from the Bengal Presidency Board, just as the Imperial Government has been distinct from the Local Government of Bengal. This has not been a feature of earlier schemes, and the suggestion that one of the Presidency Offices would be in effect the Head Office of the whole Bank has been responsible for setting up local jealousies which the present scheme ought to avoid.

In the outline constitution given above, Delhi (or alternatively Calcutta) has been suggested as the headquarters of the Central Board. Delhi is open to a good deal of obvious criticism, but has, on the other hand, some advantages. To place the Central Board at Calcutta might lead to an undue overshadowing of the Bengal Presidency Board, as well as to a confusion in the public mind regarding the relation of the two Boards to one another. The suggestion of making the Calcutta Office the Head Office would no doubt commend itself to Calcutta interests. But there is no question of this; and it is doubtful whether local Calcutta interests would welcome a Central Board, on which Calcutta shareholders would not be directly represented, in immediate proximity and with superior powers to their own Presidency Board on which local interests have ample representation. To fix the Central Board at Delhi safeguards, on the one hand, its own impartiality and, on the other hand, the complete local independence of the Presidency Boards. This location would also facilitate the attendance of the Government representative,* and would be geographically convenient both for touring on the part of the officers of the Central Board, and for attendance at meetings on the part of the assessors from the local boards.

The chief objections to Delhi are, first, that this location would place the Bank too much under the direct influence of Government, and second, that the officers of the Bank would be too little in touch with commercial opinion. The first objection is obviously not capable of a precise answer and will appeal with varying force to different persons. But it may be pointed out that there is little reason for supposing that high authorities will wish to interest themselves in the Bank's daily transactions of which they will not apart from the Government's representative on the Central Board, have any official cognisance at all: and that the Bank's independence is considerably safeguarded by its constitution, and by the complete absence of connection with the Civil Service on the part of the Governor and Deputy Governor. The second objection is partly met by the following considerations. In the first place, the Central Board is to have no direct dealings whatever with the public, to whom, therefore, so far as the transaction of business is concerned, its location will be a matter of indifference. In the second place, the Central Board would rely for its knowledge of the

* It is understood, however, that the new Comptroller of Currency is to have his headquarters at Calcutta.

commercial situation partly on the not infrequent touring of the Governor or Deputy Governor, and partly on the attendance at its meetings of the Managers of the Presidency Head Offices. Their knowledge of the *general* position would probably be more complete in this way than if they were permanently fixed at some one Presidency town. The fact that the busy seasons in different parts of India are to some extent distinct, emphasises the convenience of touring on the part of the Bank's highest executive officers.

The duties of the Central Board would be chiefly concerned with bank rate, with the remittance of funds from one Presidency to another, and between India and London, and with questions of general policy. But it might be advisable that they should also have directly under them an Inspection and Audit Department, not for the purpose of controlling the Presidency Boards and the various branches of the Bank, but as an independent check, after the event, on the nature of the business done, and as a means of rendering more actual the ultimate responsibility of the Central Board for all the Bank's transactions.

The position of the Presidency Managers in their capacity of Assessors to the Central Board requires further explanation. It would not be practicable to make them complete members of the Central Board, since this would imply more regular attendance at the Board's meetings than would be compatible with their duties at their own Head Offices. At the same time, it is desirable that they should be in close touch with the Central Board in person and not only by correspondence. The proposed scheme is intended to make it possible for them to attend the Central Board on occasions when they can conveniently be absent from their own office, and when they specially desire to place their views or proposals before the Central Board in person. The Central Board, on their part, would be able to convene from time to time meetings at which all the Presidency Managers would be, if possible, present. While the Central Board's offices and establishment must be fixed, there is no reason why the Board itself should not meet from time to time, if it should be found convenient, at various centres.

One of the main points to be emphasised regarding the relation of the Presidency Boards to the Central Board is that all questions of *individual* credit would be ordinarily within the discretion of the Presidency Boards. The general magnitude of the transactions of any kind must come within the cognisance and ultimate control of the Central Board. But the nature of the individual transactions making up the total, in general, should not. The Local Boards would thus possess substantial autonomy in the discount of inland bills and in the granting of advances. In all matters relating to individual credit they would possess the same independence as each Presidency Bank has now. They would also control the movement of funds within their own Presidency. They would, therefore, be able to conduct all ordinary business with members of the public with exactly the same degree of despatch as at present and without reference to higher authority.

3. Third, as regards the relation of the Bank to its shareholders. The chief points to be considered are the fair treatment of the shareholders in regard to their share of profits, the utilisation of the commercial knowledge and the commercial instincts of the shareholders' representatives, and the maintenance of the supreme authority of the Bank in the hands of officers who are not open to pressure on matters affecting the public policy and the general good of the commercial and banking community.

The question of profits is treated in the next section of this Memorandum. The other two considerations are dealt with in the proposed scheme, on the one hand by constituting half (or, perhaps, a majority) of each of the Presidency Boards from representatives of the shareholders and by requiring the approval of these representatives to the appointment of the Managers of the Presidency Head Offices; and on the other hand by giving the shareholders no direct representation on the Central Board, though allowing them full opportunity of access to this Board and of laying their views before it through their local Managers. It might also be proper, as in the case of the Reichsbank, to distinguish certain questions, such as the drawing up of the annual balance sheet, on which special attention should be paid to the views of the shareholders' representatives.

Such limitation of the powers of the shareholders as is proposed in this scheme may appear to Indian opinion a somewhat novel feature which is open to criticism. But it is, I think, an unavoidable consequence of the great privileges and responsibilities of a State Bank, and does not go so far as in most of the State Banks of Europe and elsewhere.

IV.

CAPITALISATION OF THE BANK AND DIVISION OF PROFITS.

There is no question but that the nucleus of the new Bank is to be obtained by the amalgamation of the capital and reserves of the three Presidency Banks.

Continental experience suggests (*see* Appendix A) that it is probably inadvisable for the Government to subscribe any part of the capital of the Bank itself. Subscriptions from the Government are not necessary (*see* what is said below in regard to proposals for an increase of capital), and would complicate rather than simplify the relations between the Government and the shareholders.

It is proposed that the assets of the three existing Banks be taken over in the following manner:—

(1) The existing assets of the Banks to be accurately valued.*

* As they stand at present in the books of the Banks, the assets are almost certainly undervalued.

(2) The reserves of each to be levelled, so as to bear the same ratio to their respective capitals, by reducing reserves and paying away the excess to the shareholders, or by increasing the reserves out of earnings as may be determined hereafter.*

(3) One share in the State Bank to be issued to shareholders for each share held in the Presidency Banks.

When this has been carried out, is any further increase of capital desirable? Earlier proposals for a Central Bank have attached a good deal of importance to an increase of capital. But this has probably been the case because these proposals have approached the question from a somewhat different point of view. The Government have often in the past given the low capitalisation of the Presidency Banks as a reason why they did not care to deposit a large part of their free balances with these banks. This objection was applicable in hardly less degree to a Central Bank which was merely an amalgamation of the existing Presidency Banks. Proposals for such a Central Bank were coupled, therefore, with proposals for an increase of capital. But the relation of the Government to the proposed State Bank will be such, that the additional guarantee which would be afforded by the subscription of further capital by the shareholders seems scarcely necessary. The advantage of the additional capital to Government would only arise in the case of the Bank's failure. In the event of so extreme a calamity, the loss by Government of 1,000,000*l.* more or less would be, relatively, of small consequence—the other results of such an occurrence would be so far more serious. The constitution of the Bank ought to ensure its being worked on such lines that the contingency of failure, in the sense of insufficiency of assets to meet liabilities, is almost inconceivable. Moreover, if failure were to result, it must be admitted, I think, that the responsibility of Government would be so great that they could scarcely remove the whole of their balances intact, leaving to the shareholders the whole burden of the loss.

The only other reason for an increase of capital is lest the Bank should suffer from an insufficiency of working capital in its daily business. I doubt if this is likely to be the case. The capital and reserves under the above scheme would amount to 5,000,000*l.*, and with the control of the paper currency and of the Government's cash balances the resources of the Bank would be very great.

If, however, it were held for any reason that some increase of capital was desirable, it would not be difficult to raise it. For example, new capital might be issued for $3\frac{3}{4}$ crores (doubling the existing capital) of which only 20 per cent. would be called up. The offer of such shares to the existing shareholders *pro rata* at a premium of (say) 100 per cent.† would be a valuable concession to

* This will present no practical difficulty, as the ratios of reserves to capital in the three Banks happen to be very nearly equal as it is.

† The existing shares of the Presidency shares stand at a premium of more than 200 per cent.

them, or the issue may even be made at par if it is considered politic to offer great inducements. It may be assumed in either case that the shares would be taken up. While some such method as this might be advantageous if the object were to afford some additional guarantee for the deposits, an insufficiency of working capital might be best met by an issue of preference shares. Power could be taken in the Bank Act to issue 5 per cent. preference shares to a considerable amount, only to be issued by degrees, if and when required. Although the issue of preference shares may appear unusual to English bankers,* and is thrown out merely as a suggestion, I do not see that it is open to objection.

It would probably be wiser not to add the reserves of the existing Banks to the capital and distribute them by way of a new issue of shares. Although this would mean, in effect, no more than a change in book-keeping, it is open to the objection that it would weaken, in appearance, the balance-sheet of the new Bank and create an unwieldy nominal capital on which to pay dividends.

It may be objected that the proposed scheme takes no account of the fact that the market values of the shares of the three Banks are not at all quite the same level.† It is not likely, however, that, when the assets have been revalued, the actual earning power of the Banks in recent years ascertained, and the necessary readjustments made by payment of cash bonuses or otherwise, so as to bring the ratio of surplus assets to capital to the same proportion for each Bank, that any appreciable difference between the position of the three Banks will be apparent. If on investigation it were to appear that the real earning powers of the Banks or the ratios of surplus assets to capital are substantially different, it would be proper to make allowance for this. But everything points to the reasonableness of taking a broad view and treating all the Banks on a uniform plan.

The question of the division of profits between the shareholders and the Government raises a problem of a good deal of difficulty. Apart from the question of prestige, the management of the note issue and of the Government balances will provide the Bank with a considerable source of revenue, likely to grow in the future, in the fruits of which the Government must obviously share.

One method would be for the Bank to pay for the prestige by performing certain Government services without remuneration, and for the use of the public balances by a sum dependent on their amount and the bank rate; and for the Government to retain the estimated profits of note issue. This method would not be satisfactory. There is no certainty that the arrangement would work out equitably as between the shareholders and the Government. And the chief objection to it is in the inherent difficulty of sepa-

* Nevertheless the "A" shares, created this year by Barclay's Bank, are not very different from preference shares.

† Market quotations, August 1913:—Bank of Bengal, Rs. 1,700; Bank of Bombay, Rs. 1,670; Bank of Madras, Rs. 1,440. In each case the quotation is for Rs. 500 shares.

rating the business of the Bank into compartments, and of deciding how much of its net profit it has derived from each source. Such a method of division of profits runs counter to what ought to be an important principle of a central Bank—the regarding of the Bank's operations *as a whole*.

In the case of the Bank of France, the Government receives no direct share of the profits of the Bank, but gets its benefit in a rather complicated way by a number of indirect services and payments. But the normal continental arrangement is one in which the Government receives its advantage partly by the free performance of services on the part of the Bank, partly by a tax on the note issue, and partly by a share in the profits. The arrangements which govern the distribution of the profits of the Reichsbank are given, as the leading example, in Appendix C. The details of the German plan are not suited to the Indian conditions; but the general idea running through it is, I think, a good one.

In the case of the Imperial Bank of India, I suggest something of the following kind:—

1. The Bank shall perform without special remuneration the following duties:—

(*a*) To purchase gold bullion at a notified rate, to issue (but not mint) gold and silver, to manage the note issue and the custody of the Paper Currency Reserve.

(*b*) To accept payments and make disbursements on behalf of the Government (Imperial and Local) at all places where the Bank has set up a branch.

(*c*) To manage the Government debt in India.

2. The Bank shall pay to the Government annually a sum equal to the present income from the *sterling** investments now in the Paper Currency Reserve, and from such investments as may be transferred from the Gold Standard Reserve in exchange for gold (*see* below). The Bank shall also pay over the proceeds of any tax chargeable on excess issues of paper currency (*see* Regulation of Note Issue, below).

3. The annual net profit of the Bank, after due allowance for depreciation, preference dividend (if any), etc., and after deducting payments to the Government under (2) above shall be dealt with in the following manner:—

(*a*) A regular dividend of 10 per cent. on the ordinary capital to be distributed among the shareholders, being made up to this amount from the reserve, if the net profits fall short of 10 per cent.

(*b*) Of the remainder, after payment of 10 per cent. two-fifths to be transferred to the reserve when this remainder is

* For the treatment of the *rupee* investments now in the Paper Currency Reserve, *see* below.

not more than 20 per cent. of the capital, and one-third when it exceeds 20 per cent.

(c) The divisible surplus, after deductions (a) and (b) shall accrue to the shareholders up to an additional 5 per cent. of their capital, and thereafter to the shareholders in the proportion one-third, and to the Government in the proportion two-thirds.*

The effect of these provisions is shown in the following table:—

In Percentages of the Capital.

Net Profits, Percentage.	Percentage to Shareholders.	Percentage to Reserve.	Percentage to Government.
8	10	—2	...
10	10	...	...
12	$11\frac{1}{3}$	$\frac{4}{5}$	...
15	13	2	...
16	$13\frac{3}{5}$	$2\frac{2}{5}$	...
18	$14\frac{4}{5}$	$3\frac{1}{5}$	...
20	$15\frac{1}{3}$	4	$\frac{2}{3}$
22	$15\frac{11}{15}$	$4\frac{4}{5}$	$1\frac{7}{15}$
25	$16\frac{1}{3}$	6	2
28	$16\frac{14}{15}$	$7\frac{1}{5}$	$3\frac{13}{15}$
30	$17\frac{1}{3}$	8	$4\frac{2}{3}$

At present the net profits are approximately 17 per cent., of which 14 per cent. is divided and 3 per cent. placed to reserve. Under the above scheme the Government receives no share until 15 per cent. is being divided amongst the shareholders and nearly 4 per cent. placed to reserve. Thus, the position of the shareholders is almost certainly improved, and the Government take no appreciable part of the profits unless the control of the paper currency, the custody of the Government balances, and the prestige attaching to a State Bank have the effect of raising the profits very greatly above their present level. Those who believe that the establishment of a State Bank may have a very beneficial effect on Indian commerce and banking, will think it wise to facilitate such a course by a fairly generous offer to the existing shareholders.

One or two points may be added.

* Provision should probably be made for an increased proportion to Government and diminished proportions to the shareholders and to reserve, in the event of the net profits ever exceeding 30 per cent.

There has been a wise provision in the successive arrangements between the State and the Bank of France, by which the Bank is bound to open a certain number of additional branches within a given period of years. This undertaking is reckoned, as it were, as part of the payment made by the Bank for its privileges. In the case of the Bank of India, I suggest that while the Presidency Boards shall have discretion to open branches wherever they wish, they shall also be required to open them at the request of the Central Board, and that it shall be the declared policy of the Central Board to open branches, as rapidly as opportunity offers, and the necessary staff and organisation become available, at most places where there is now a District Treasury.*

There must also be conditions, as in the constitution of the Reichsbank, providing for the revision of relations between the shareholders and the Government.

1. The Bank Act shall be reviewed at intervals of 10 years, and shall be subject to equitable revision at the option of Government or at shorter intervals with the concurrence of the shareholders.

2. At each decennial revision the Government shall be free to take over the whole goodwill and assets (including the reserve) of the Bank at 25 years' purchase of the average of the sums payable to the shareholders in the five years preceding.

The first provision may seem to place the shareholders somewhat at the mercy of the future good faith of the Government. But it is difficult to limit the authority of a sovereign power. Every institution, however purely private, is ultimately dependent on the Government's equitable regard for existing interests. From a Government which was deliberately prepared to revise the charter *inequitably*, even a Presidency Bank would hardly be safe.

The profits of an Indian Bank are likely to be very fluctuating. It might be advantageous, therefore, if the shareholders were competent to form a reserve for the equalisation of dividends, which should remain wholly their own property in all circumstances. This might be invested in Government paper, or held by the Bank on payment of interest at a rate equal to the average bank rate during the year.

V.

REGULATION OF THE NOTE ISSUE.

The chief object of the principles set up in 1844 to govern the Bank of England's note issue was the certain avoidance of those evils attendant on an inconvertible and inflated paper currency,

* These are 271 in number, while the Presidency Banks have at present only 35 branches between them. It will naturally take some time, therefore, to complete this policy of expansion.

of which the history of the previous half century had contained notorious instances. In attaining this object by too rigorous a set of rules the utility of the note issue was destroyed. The main function of the Bank of England's notes at the present time, apart from a very few special types of transaction, is to supply the Joint Stock Banks with a convenient form of bullion certificate more easily handled than bullion itself. The inconveniences which would otherwise have arisen have been avoided, however, by the great development of the cheque system.

Abroad the Bank of England's principles have found no imitators. But in India they were adopted in 1860 and still persist. The effect of their rigour is not moderated by any widespread use of cheques. Many authorities are now agreed that some development of elasticity in the note issue is, therefore, required.

When we look to the experience of other countries, of which much has now accumulated, as to how this elasticity can be best obtained, the following alternatives are before us:—

(i) A fiduciary issue fixed in *amount*, as in the case of the Bank of England, but with power to exceed it (until the cash falls to a certain minimum *proportion*) on payment of a tax. This is the system in Germany and elsewhere.

(ii) A fiduciary issue fixed in *proportion* to the note issue.

(iii) As in (ii), but with power to exceed the proportion on payment of a tax.

(iv) No rules but the discretion of the bank of issue to govern the amount of the reserve, but a limitation to the aggregate issue of notes. This is the system in France, where the maximum placed on the aggregate issue has been raised from time to time whenever the actual issue showed signs of approaching it.

In the choice of a system for India, the fourth of these alternatives can be put on one side. The second ought to be neglected also. For on this system, when once the prescribed proportion has been reached, not a single additional note can be encashed without a breach of the Bank Act; for if one note is cashed, the fiduciary issue, being the same as before while the cash is less, must exceed the prescribed proportion.

Our choice lies, therefore, between (i) and (iii). Between these two there is not really any very substantial difference. For when the *amount* is fixed from time to time, it is naturally fixed so as to be some reasonable *proportion* of the total. In the case of a country with a rapidly growing note issue, the advantage lies, I think, with (iii); otherwise frequent legislative changes will be required. Germany adopted (i) in the first instance, because it seemed less of a break with the Bank of England's system; but, as their note issue has developed, frequent legislative changes have

been necessary to raise the amount of the untaxed fiduciary total, so as to make it a reasonable proportion of the whole circulation.

In what follows, therefore, I propose for India a variety of (iii):—

Proposed Rules to govern the Indian Note Issue.

1. Up to 40 per cent. of the gross* circulation of notes may be held in a fiduciary† form without payment of tax, the balance being held in cash (gold or rupees).

2. Up to 60 per cent. may be held in a fiduciary form, on payment of a tax to the Government at the rate of 5 per cent. per annum on the excess of the fiduciary issue above 40 per cent. of the total circulation.

3. The proportion, in a fiduciary form, shall *never* exceed 60 per cent., *i.e.*, the proportion of cash shall never fall below 40 per cent., save that the Secretary of State in Council shall have authority, in emergency, to suspend the provision of the Bank Act which enjoins this.

The propriety of the particular percentages here proposed is, of course, a separate question from the propriety of the principle. In judging of it, we must bear in mind that, while the percentage given in (i), *i.e.*, 40 per cent., is what one would expect the Bank to work up to not infrequently, the percentage given in (2), *i.e.*, 60 per cent., is an outside limit, which the Bank would never work near to except, possibly, on occasions of dangerous crisis. For if it ever worked near to 60 per cent., the encashment of a few notes would put it in danger of having to apply for a suspension of the Bank Act. Thus, if the absolute maximum is fixed in the form of a *proportion*, plenty of margin must be allowed, and the maximum proportion must be fixed well above what would be thought the highest reasonable proportion for normal times. If comparisons are to be made, this figure is considerably more cautious than the corresponding figure for the Reichsbank. The legal maximum proportion for their fiduciary issue is 67 per cent., but as the so-called "cash" includes some items which are not cash at all, the corresponding figure may be put at 70 per cent. In September 1911 the Reichsbank actually worked up to 57 per cent., holding only 43 per cent. in cash at the end of that month. In September 1912 they worked up to 50 per cent. This year the authorities have felt that to work up to such a figure in comparatively normal circumstance may be incautious, and they have somewhat strengthened their position. But no one has suggested that they should lower the proportion up to which they are *legally entitled* to work.

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* This is interpreted below to include the notes held by the Bank itself in reserve, as well as the "active" circulation.

† *What* fiduciary form, is discussed below.

I am clear, therefore, that it would be unwise, in the case of India, to fix the legal maximum below 60 per cent. (*i.e.*, to fix the legal minimum of cash above 40 per cent.). Plenty of "play" ought to be allowed for occasions of emergency, when even a suggestion of a suspension of the Bank Act might provoke panic. But it is equally clear that the *normal* maximum ought to be well below this amount. For this, reliance must inevitably be placed on the judgment of those in authority at the Bank, and not on legal safeguards.

The propriety of the figure, namely, 40 per cent. fixed in (1) is much more open to question. It partly depends on how much tax is to be paid on excess issues. I believe that it would be safe to allow the Bank to work up to this amount before any pressure need be put on the authorities, other than their own judgment, to raise the bank rate. But no principle is involved in the choice of this particular figure.

The existing fiduciary issue was 24 per cent. of the *average* gross and 26 per cent. of the *minimum* gross circulation in 1911-12; and the corresponding figures (estimated) in 1912-13 were 21 per cent. and 24 per cent. Precise comparison with the Reichsbank is not possible, because at any given date their fiduciary issue is a fixed amount and not a fixed proportion; but a study of the figures suggests that 40 per cent. is about the equivalent of German practice.

We may take the present normal minimum gross circulation at about 60 crores of which from 42 to 45 crores is active (*i.e.*, excluding Government Treasuries and Presidency Banks); of this 14 crores is now held invested. The notes now held in Government Treasuries, as well as those now held in the Presidency Banks, would be held in the reserve of the new Bank, although, presumably, the former would not be maintained at their present magnitude. We may assume that the Bank, like the Bank of England, would hold its whole cash reserve, apart from till money, in notes (*see* below).

Now, if in the slack season there were 40 crores in circulation and 20 crores in the Bank's own reserve, the fiduciary portion could rise without payment of any tax to 24 crores.

If in the busy season the active circulation rose to 45 crores and the reserve fell to 15 crores, the fiduciary portion could rise, as before, to 24 crores without payment of tax, and 4 crores higher on payment of a 5 per cent. tax on the excess 4 crores, a safe margin being still preserved below the permissible maximum of 36 crores. Recent experience shows that the circulation would frequently rise higher than this.

This scheme would, therefore, put very large funds at the disposal of the Bank. Nor would any risk be run of inability to encash the notes, as is shown in the following table, which gives

the percentage of cash to active circulation in each of the hypothetical cases instanced above and in some others also:—

In Crores of Rupees.

Active Circulation.	Notes in Reserve.	Fiduciary Issue.	Cash.	Percentage of Cash to Active Circulation.
40	20	24	36	90
45	15	24	36	80
45	15	28	32	71
50	20	28	42	84
50	20	30	40	80

Further, probably 10 to 15 crores of the reserve held against the fiduciary issue (*see* below), would be held in sterling securities or sterling bills, capable of being realised in London. Thus more than 100 per cent. of the active circulation would be held either in cash or in sterling securities.

Finally the existence, quite apart from the Paper Currency Reserve, of a large sum in gold coin (if proposals to this effect are adopted) in the Gold Standard Reserve must be borne in mind when the possibility of grave emergencies is in question. In all ordinary times the existence of the Gold Standard Reserve should be treated as irrelevant to the proper magnitude of the Paper Currency Reserve; but against very grave emergencies, when the Government's guarantee of the note issue (*see* below) may possibly be required, the coin in the Gold Standard Reserve would provide a temporary bulwark, pending the realisation of the sterling securities.

It would hardly be reasonable, I think, to criticise the above scheme on the ground of insecurity to the holders of notes.* These figures also bring out the essential wastefulness of the present system. More than 100 per cent. of the *active* circulation is now held in cash.

So far merely the amount of the fiduciary issue has been discussed, and not the form of the securities to be held against it. At present 10 crores are held in rupee paper and 4 crores on Consols. It is suggested below that 6 crores in Consols should be transferred, in exchange for sovereigns, from the Gold Standard Reserve. This would make 20 crores in all of permanent investment, and this is certainly the highest figure at which the permanent investment ought to stand at present; perhaps it is too high.

The security for the fiduciary issue, beyond the 20 crores of permanent investment, should consist of approved securities (Gov-

* The normal proportion of cash to active circulation would be higher than in most European systems of note issue, higher even than in the case of the Bank of France.

ernment paper and possibly a few others) temporarily transferred from those held by the Bank on its own account or pledged with it by its customers, and of bills of exchange, both sterling and rupee. The securities, pledged with the reserve, should be taken at a safe margin below their market value.

For the fluctuating part of the fiduciary reserve, bills of exchange having two good names to them are far preferable to securities, if they can be obtained. They come into existence precisely at the moment when there is most need for additional currency and are liquidated when this need comes to an end. Securities, on the other hand, must be carried by somebody all the year round. Moreover the amount of securities forthcoming is likely to be limited. Suppose a Bank or a firm can get money at 5 per cent. on the security of Government paper and use it at 6 per cent. for three months in the year, then on the average of the year they make about $4+\frac{1}{4}(6-5)$ per cent., *i.e.*, $4\frac{1}{4}$ per cent. It suits a Bank to hold some Government paper. But the above calculation show that a point would soon come when this would not pay. Bills, on the other hand, do not lock up money all the year round. To discount at 6 per cent. and rediscount at 5 is a much more profitable transaction for a Bank than the transaction outlined above.

Experience elsewhere shows that the elasticity of notes based on Government paper is very limited, and that bills are the essentially suitable backing to that part of the note issue which is fluctuating and called into existence in the busy season only. The amount of Government paper which it suits the banks to hold, since it must be held all the year round, is not suddenly expansible; nor is it easy for them suddenly to liquidate their holdings, or, from the Government's point of view, desirable that they should. The American note issue, which is based on Government paper, has proved hopelessly inelastic, and it is one of the principal objects of the projected reforms in that country to introduce an elasticity based on the discount of the trade bills.* In all European countries bills are the pivot on which the whole meaning and utility of the note issue essentially turns.

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* The following quotation from a recent communication to *The Standard* about the less well-known experience of Cape Colony is instructive:—"The Cape legal tender issue represents the only attempt to establish a scientific system in South Africa, but it becomes increasingly clear that this system is not suited to satisfy the larger requirements of the Union. The application of this system to the Union would necessitate, on the part of the banks of issue, the investment of additional funds in Government securities as cover, which fact, in its turn, would narrow the already small margin between deposits and advances, and thus lessen the Bank's power to grant facilities. This system has already proved inelastic, despite its limited range, a fact in itself proving its unsuitability for adoption as the note currency of the Union. Despite the demand for currency by trade during the last few years, the Cape circulation has rarely exceeded 1,200,000*l*., although as long ago as 1891 experts placed its natural level at 2,000,000*l*. . . . . In short, the Banks are finding more profitable means of investment for their funds than Government securities, and the Cape note circulation consequently does not expand."

The only question is how far bills of a kind suitable to the portfolio of a State Bank would be forthcoming in India. It might be a matter of time before they would be available to the full extent which is desirable.

This leads us to the question of the relations of the State Bank to other banking institutions. The State Bank ought to aim, I think to the greatest possible extent at *re-discount* business. So far as possible, that is to say, it should aim at filling its portfolio with trade bills which have passed through the hands of another Bank or shroff or marwari of high standing and have received their endorsements. This seems to me to be the right channel through which the accommodation newly available should filter down to the great mass of Indian traders. The State Bank would have on its list certain Banks and private native financiers of high standing who would be amongst its regular customers and for whom in general it would be prepared to rediscount freely.

The power of re-discount might prove a powerful aid to the development of Indian Joint Stock Banks on sounder lines than hitherto, and involve at the same time a valuable check on them. For, on admitting a Bank to the re-discount list, the local manager of the Presidency branch would require, from time to time, to examine somewhat carefully, in confidence, the Bank's position; and the risk of losing its position on the re-discount list might act, to some extent, as a deterrent to rash banking.

Apart from this check, the creation of a re-discount market would render such Banks most vital assistance. Indeed I am doubtful how far it is possible for them to develop on really sound lines without it. The smaller the Bank, the larger the number of its branches, and the less developed in banking habits the country in which it acts, the higher in proportion to its resources ought its free cash reserves to be. If a newly founded Indian Joint Stock Bank were to keep sufficiently large cash reserves to provide against all reasonable contingencies, it could scarcely hope to earn adequate dividends. At present, apart from cash, such a bank is very short of modes of so employing its resources as to keep them fairly liquid. There is no one to whom they can safely lend at call. A Bank which pays from 4 to 6 per cent. to its depositors cannot be expected to hold large quantities of high-class investments yielding barely 4 per cent. Such bills as they may get hold of must probably be held until maturity. Inevitably they tend to lock up in industrial enterprise a higher proportion of their resources than is wise. Some recent failures seem to be due to a different cause, not so much to the locking up resources as to advances against *worthless* security. But in really bad times comparatively well conducted institutions may find themselves in difficulty, not because their security is worthless, but because it is temporarily unrealisable.

If a State Bank were to encourage the transaction of business by means of trade bills, through making bills easy things against

which to obtain advances, native Banks might hope in time to obtain more of them for their portfolios and would have something which they could turn into cash at need by re-discount.

In this matter of the development of the use of trade bills, however, I am looking not so much to the immediate future as to the ultimate development of Indian banking practice on sound and well-tried principles.

Two further points in regard to the note issue remain for discussion.

The notes must, I think, remain Government notes in the sense that the Government, in addition to the Bank, guarantees them. In this case they could preserve their present form and appearance unchanged, *i.e.*, they could remain, as they are at present, Government promissory notes payable on demand at certain places in legal tender money.*

This should allay suspicion without laying on the Government any real additional burden. For if the Bank were, by a violent chance, to get into difficulties, there cannot be the least doubt that the Government would have to maintain the solvency of the note issue whether they had formally promised to do so or not.

The remote contingency of the Government's having to give temporary effect to this guarantee could be properly laid on the Gold Standard Reserve. For, although an exchange crisis changes the form of the Gold Standard Reserve, it in no way affects the total amount of legal tender money held there.

The Government's guarantee carries with it as a necessary consequence—probably desirable on general grounds anyhow—the allocation of specific assets as cover for the note issue and a division in the Bank's published accounts between the Issue and Banking Departments. Rather oddly, this feature of the Bank of England's arrangements has not been generally imitated abroad. In the normal continental type, no distinction is made between the reserve held against the note issue and the reserve held against other banking liabilities. Legally, the whole cash reserve is treated as being cover for the notes; and no notes are held by the Bank itself, so that there is no distinction between total and active circulation.

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* In 1900 the Government of India in a despatch (18th January 1900) to the Secretary of State regarding proposals for the transfer of the note issue to a central Bank, wrote:—"As any change in the form of the note might involve temporary contraction in the paper circulation, as change in such matters is peculiarly undesirable in India, and as the reserve would be under the supervision and control of Government, we should have no objection to the notes continuing in their present form, with the possible addition of the name of the Bank and the counter signature of the officer employed to supervise the reserve. We are of opinion, though not forgetting the objections that have been previously raised to such a course in India, and indeed recently adverted upon by so high an authority as Lord Northbrook, that there is nothing in the peculiar circumstances of India to prevent the note issue being transferred to a Bank. We are, moreover, disposed to believe that it is through the agency of a Bank that the note issue may have a larger development in India."

Among its assets the Bank must hold a sufficient quantity of security of a kind which is legal backing for the fiduciary part of the circulation; but no part of the Bank's securities is specifically allocated to the note issue.

In this respect the Bank of England provides India with the better model. In the published accounts a distinction should be made between the Issue and the Banking Departments thus (with hypothetical figures)*:—

Issue Department.

	Crores.		Crores.
Gross circulation of notes outstanding	65	Government Book Debt	10
		Consols	10
		Security pledged with Issue Department:—	
		Approved securities, Bills of exchange	6
		Gold	15
		Rupees	24
			65

Banking Department.

Capital, etc.	Notes in Reserve . . 20
Deposits, etc.	Investments.
	Bills.
	Advances, etc.

Several details in this require explanation:—

1. The "Government Book Debt" corresponds to the 10 crores of Government rupee paper now held in the Paper Currency Reserve. I propose that this rupee paper should be cancelled, and be replaced by a Government book debt bearing no interest. This corresponds to the Government book debt due to the Bank of England, and avoids fluctuations in accordance with the market value of rupee paper.

* In a continental Bank these two accounts would be merged, the circulation of notes would appear as 45; no notes would appear on the asset side of the banking account; and the investments and bills in the two departments would be lumped together. This would make the proportion of cash to circulation appear to be 87 per cent., instead of 60 per cent. as in the above. This difference in account-keeping, which makes the position in continental Banks appear stronger than it really is, must be kept in mind in making comparisons.

2. The Consols (four crores from the existing Paper Currency Reserve and six crores from the Gold Standard Reserve in exchange for gold) would be taken over at market value. The initial book value should in the event of subsequent depreciation, be written down to market value annually, but should not be written up, in the event of appreciation, until market value exceeds book value by 10 per cent., and then only by the excess beyond 10 per cent.

3. The approved securities, pledged with the Issue Department should show a margin of 5 per cent.; the bills of exchange should be taken at par, less rebate.

4. So long as the fiduciary issue does not exceed the untaxed maximum, it will make no difference to the Bank's profits whether they make up the gross circulation to the untaxed maximum by transfer of securities to the Issue Department and increase the notes in reserve correspondingly, or let the gross circulation fall below the untaxed maximum by a reduction of the notes in reserve. When the untaxed maximum is passed it will pay the Bank better to let the notes in reserve fall somewhat, as they will avoid payment of tax by the amount of the fall. This circumstance is, no doubt, the explanation of the continental method of account-keeping. But, provided the Bank is governed by caution, the extent to which they will feel willing to reduce their notes in reserve in order to avoid payment of tax will be no more than is reasonable. And even if the notes in reserve sank to zero, the position, measured by percentage of cash to note issue, would still be as strong as in a continental Bank.

5. As the Government guarantees the note issue, the securities and cash belonging or pledged to the Issue Department will become their property, so far as required for meeting liability on the notes, in the event of difficulties. But apart from the interest on the 10 crores of Consols, the annual profits of the note issue (and any excess in the value of the assets of the Issue Department over its liabilities) are the property of the Bank.

In concluding this section, a word may be said about the Circle System. There seems no reason why it should not be abolished. There should be a legal right of encashment of notes of all denominations at a small number of prescribed offices of the Bank; and all other offices, though under no legal obligation, should be authorised to encash notes whenever they can do so without embarassment. It is to be hoped that, as time goes on, the occasions when they would not find it convenient to encash them would become increasingly rare. The notes are, of course, legal tender, and must be accepted *in payment* by all branches of the Bank.*

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* *Cf.* § 18 of the German Bank Act:—

The Reichsbank is required to redeem its notes to bearer in German currency (N.B., in silver or gold at the option of the Bank):—

(*a*) At the main office in Berlin, and

(*b*) at its branch offices *as far as the cash and money exigencies of the latter permit.*

VI.

THE LONDON OFFICE AND REMITTANCE.

With this section we enter on a debatable part of the subject, which is largely independent of the rest.

No important object would be served by allowing the Bank to compete with the Exchange Banks in attracting deposits in London. Nor is there any clear advantage (sufficient to counterbalance the opposition which would be aroused) in allowing it to enter into the regular business of trade remittance by buying trade bills in both directions. Such competition with the Exchange Banks is in no way necessary to the prime objects of a State Bank.

But it is desirable that the Bank should be free to carry out the Secretary of State's remittance in the most satisfactory and economical way, and to hold balances in London and use them in the London market. It is also desirable that the Bank should not be unduly fettered in providing private remittance on London for its Indian customers. If at some up-country branch of the State Bank a customer wished to buy a draft on London for 50*l*., it would be absurd if the Bank had to refuse to do this business for him.

The London Office of the State Bank would be, therefore, a comparatively small affair. It would have no direct dealings with the public, only with the Secretary of State, the Money Market, and other Banks. The Secretary of State would continue to do his ordinary banking business with the Bank of England and to maintain a balance there; and it would be the business of the London Office of the State Bank to keep him in funds. The main point for discussion is as to what the best machinery will be for carrying out the remittance transactions wherewith to keep the Secretary of State in funds.

The methods of effecting remittance are two: by selling drafts on India in London, as at present, and by buying sterling bills in India. There will be great advantages in leaving both these methods open to the Bank. The due safeguarding of the interests of existing Banks is not incompatible with this. The State Bank should be precluded from buying sterling bills in India, *except from other Banks:* its dealing in sterling bills, that is to say, should be entirely a re-discount business of bills bearing the endorsement of another Bank. The sale of rupee drafts in London might be by tender as at present, but it would probably be a better plan for the London office of the State Bank to quote rates for bills and transfers to applicants. In this matter, also, the State Bank should be confined to dealing with other Banks and not direct with the trading public, or (as an alternative, if this proposal should be deemed a hardship to certain important houses which tender direct for Council bills at present and do not, as it is,

do their business through an Exchange Bank) should sell for not less than a lakh at a time.*

The Exchange Banks would thus have two ways of putting themselves in funds in India, corresponding to the two ways open to the State Bank of providing themselves with funds in London. They could re-discount sterling bills in India or buy (as at present) rupee drafts in London. The existence of the first method, as well as the second, might sometimes prove a real advantage to them. The State Bank would naturally quote rates for re-discount in India and for the sale of drafts in London which would make it worth the while of the Exchange Banks to take the course most convenient at the moment to the State Bank. If at a season when the Exchange Banks were wanting funds in India, the Secretary of State was also in need of additional cash in London, inducement would be offered to the Exchange Banks to buy drafts; and if the Secretary of State's needs were mainly in the future, inducement would be offered to the Exchange Banks to re-discount sterling bills in India, which could be held by the State Bank until the Secretary of State wanted the money.

The price which would be paid for sterling bills in India by the State Bank would necessarily be governed by the London rate of discount for such bills taken in conjunction with the rate of exchange, not by the local rate for rupee bills. Thus, if the London rate of discount for three months' sterling bills of this type were $4\frac{1}{2}$ per cent. and exchange stood at 1*s.* $4\frac{1}{16}$*d.*, the corresponding rupee price for three months' sterling bills offered in India would be approximately 1*s.* $4\frac{1}{4}$*d.* per rupee. Any concession on this price offered by the State Bank in India, so long as its London office was able to enforce 1*s.* $4\frac{1}{16}$*d.* as the rate for telegraphic transfers on India, would be an inducement to the Exchange Banks to re-discount in India rather than re-discount in London and then buy telegraphic transfers there. At the same time such a policy might be advantageous to the State Bank itself. As the London rate of discount is frequently below the Indian rate, this policy would sometimes involve re-discounting sterling bills at what would be, in effect, a lower rate than was being allowed on rupee bills. But this could afford no reasonable ground of complaint to Indian merchants. For the money thus employed would not have been available in any case for rupee advances. The alternative to the use of these funds for the re-discount of sterling bills would be the remittance of them to London through the encashment of telegraphic transfers and their employment on the London market.

There can be no question that the method outlined above is the most perfect method of effecting remittance from the purely financial point of view, and also that it will be more easy of favourable explanation to the public, for the following reasons. At present the train of events is a very complicated one. The Exchange

* At present, however, "specials" are often sold by the Council for much less sums than this.

Banks buy sterling bills in India, which they bring to London and re-discount, in part, in the London Money Market. With the proceeds of re-discounting they buy Council drafts or transfers from the Secretary of State, which, when encashed in India, replace the funds which the Banks have paid out in originally buying the sterling bills. The Secretary of State lends the proceeds of selling Councils, until such time as he has need of them for his disbursements, either to the Exchange Banks themselves or to other constituents of the London Money Market, by whom the money is largely used for re-discounting bills either for the Indian Exchange Banks or for similar institutions working in other countries. If, on the other hand, as is proposed above, the State Bank were to re-discount sterling bills for the Exchange Banks in India and hold the bills until the money was actually wanted by the Secretary of State, the whole (or nearly the whole) of the floating sterling resources would be directly employed in the assistance of India's foreign trade, instead of assisting it in a very slight and indirect way through general help given to the London Money Market. No one could justly maintain that money was being diverted away to purposes wholly unconnected with India. In the second place the floating sterling resources would earn a higher rate of interest than at present, partly through the elimination of an intermediate profit and risk, and partly because three-month bills could safely be taken in many cases in which money is now lent by the broker for only six weeks.* And, in the third place, these advantages would not be counterbalanced by any increase of risk. Whenever it turned out that the Secretary of State was in need of funds somewhat sooner than had been anticipated, it would always be possible to re-discount at the Bank of England on favourable terms sterling bills, domiciled in London, and bearing the endorsements both of the State Bank of India and an Exchange Bank. Apart from the ease of rediscount, such bills would afford the finest possible security, and the Bank could only suffer loss in the event of the simultaneous insolvency of the Indian drawer, the London acceptor, and the Exchange Bank through which the Bill had been negotiated.†

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* Because, if it turned out that the money was wanted after six weeks, the bills could be re-discounted at the Bank of England. At present money is not lent for more than six weeks and seldom for so long, because of the remote contingency, which always exists, that it might be wanted by then. In giving evidence, the Secretary of State's broker seemed to be unaware that the *average* rate for three months' money is higher than the *average* rate for six weeks' money (*i.e.*, that a man who always lent for three months would make more on the average than a man who always lent for six weeks); but this is a well-known fact, or, if not well known, easily ascertained by reference to the records of recent years.

† The smallness of the risk involved is well illustrated by some figures which have been calculated for the Reichsbank. They estimate that since their foundation in 1875 their average loss on bills is well under one-3,000th part. Many of these bills are for small amounts, and without the extra guarantee of re-discount, both drawer and acceptor are in the same country and subject to similar contingencies, and the period in question is long enough to include several occasions of crisis. The average loss on re-discounted sterling bills could hardly amount to as much as one-10,000th part.

This proposal is in no sense novel, and is merely an adaptation to Indian conditions of the practice most usually followed by foreign countries. A foreign Bank or Government, which wishes to keep floating resources in a sterling form, generally utilises for the purpose so far as it can its portfolio of sterling bills negotiated in its own country.

The Exchange Banks might be further guaranteed against ordinary trade competition by restricting the State Bank in its London re-discount business to the Bank of England.

The above proposals together with a few further points of detail can be summarised as follows:—

1. The Indian offices of the State Bank shall be permitted to supply their own customers with sterling remittance, but in the purchase of sterling *trade* bills they shall be confined to the re-discount of such bills for other Banks.

2. The London office of the State Bank shall have no direct dealings as a banker with the general public. Its business shall be confined to:—

(*a*) The sale to other Banks* of drafts and telegraphic transfers payable at its Indian offices.

(*b*) The re-discount of sterling bills at the Bank of England.

(*c*) Borrowing for short periods from the Bank of England.

(*d*) The loan of funds on the London Money Market.

(*e*) The replenishment of the Secretary of State's funds at the Bank of England.

(*f*) The flotation of sterling loans on behalf of the Secretary of State.

To these functions another might possibly be added, namely, the management of the Secretary of State's sterling and rupee debt in London. But there are considerable advantages in leaving this with the Bank of England provided the charges made by them are not deemed excessive.

It remains to discuss the management of the London office.

There is some slight danger that through its close connection with the Secretary of State and the weight of authority on its Board, this office might tend to become too influential and important. This is sufficiently guarded against perhaps by the close limitations of its functions. It will have authority, of course, in regard to purely London questions, such as the employment of balances in London and advice as to the issue of sterling loans, but the only Indian question in regard to which it will be in a position to give authoritative advice will be the purchase in India of sterling bills.

The London Board will to a certain extent take the place of the present Finance Committee of the Secretary of State's Council,

* *See also* the alternative proposal, above.

and may be expected to be in much closer touch with the India Office than is likely or desirable as between the Central Board and the Government of India. Its creation will fit in very well with Lord Crewe's recent proposals for a reorganisation of his Council, on which it will not be easy in future, as I understand his scheme, to find room for more than one financier. Room can be found on the London Board for those other financial advisers, the addition of whom to the Finance Committee has been advocated by several witnesses.

The London Board, which would not include the manager of the London Office, might consist of the Financial Secretary at the India Office (or the Permanent Under-Secretary or Assistant Under-Secretary when either of these is possessed of financial experience), the Member of the Secretary of State's Council specially attached (under Lord Crewe's scheme) to the Financial Department, a representative of one of the larger mercantile houses concerned in the India trade, and two other members of financial or banking experience (one of whom perhaps might be, in general, primarily of Indian Experience and the other of London experience).

VII.

OTHER FUNCTIONS OF THE BANK.

Some of the functions already discussed, together with one or two others, may be summarised:—

(1) The Bank will perform the same functions that the Presidency Banks perform now, with relaxation, in some particulars, of the existing restrictions.

(2) It will hold as Government banker, without payment of interest, the balances now held in the Reserve Treasuries and in London, with the exception of an emergency reserve of 1,000,000*l.* which would be retained by Government in India (as proposed by Mr. Abrahams), and of that part of the London balances held directly in the name of the Secretary of State at the Bank of England. It will also hold the Government balances at all places where the Bank sets up a branch.

(3) It will manage the Note Issue on terms outlined above, and, with the exception of certain payments to Government, will enjoy its profits.

(4) It will manage the Government debt in India; and it would probably prove advantageous to entrust it with the issue of new rupee loans.

(5) Its functions in regard to remittance and the duties of the London office have been discussed above.

The following duties should *not* be entrusted to it:—

(1) The management of the Mint.

(2) The custody of the Gold Standard Reserve.

But when the Gold Standard Reserve is brought into play for the support of exchange, the Bank should act, under the Government's orders, as the Government's agent in the matter.

Something may be said in this connection about the position of the Gold Standard Reserve in the event of the establishment of a State Bank.

In the immediate past the stability of the rupee has been supported both by the Gold Standard Reserve and by the Paper Currency Reserve. This has been necessary because the former reserve has not been quite strong enough to bear the burden by itself. But as a permanent arrangement it ought not to be necessary; or, at any rate, the Paper Currency Reserve ought to be used for this purpose to only a limited degree. The ideal to be worked up to is a state of affairs in which the Gold Standard Reserve is held by the Secretary of State for the *main* purpose of supporting exchange and is adequate to this purpose, and in which the Paper Currency Reserve is held by the Bank and is controlled *mainly* with an eye to the internal affairs of India. The Gold Standard Reserve, in this case, should be governed by ultra-conservative methods, being held in gold to a far greater extent than at present; while the Paper Currency Reserve should be ruled by more commercial considerations, and a much smaller proportion than at present held in actual cash.

Although the custody of the Gold Standard Reserve and the ultimate responsibility for the maintenance of exchange must remain, in the most direct manner, with the Secretary of State, he should use the Bank as his agent in the actual sale in India of sterling drafts on London on the occasions in which the Gold Standard Reserve is brought into play for the purpose for which it exists.

The moment at which this reserve is brought into play ought not to depend, I think, upon anyone's discretion, but should be governed by rule. There should be a notification, that is to say, that the Government will at all times sell, through the Bank as its agent, sterling bills on London at 1*s*. $3\frac{29}{32}$*d*. When advantage is taken of this it will be the business of the Secretary of State to put the London office of the Bank into funds wherewith to encash the bills thus sold.

The Gold Standard Reserve, while primarily held for the support of exchange, should not be legally earmarked for this sole purpose. It can properly be regarded (*see* above) as constituting, under certain conditions, an ultimate safeguard and guarantee of the convertibility of the note issue.*

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* The propriety of this might be brought out further by showing that in a future crisis the convertibility of the note issue and the support of exchange may not always prove to be entirely distinct problems.

VIII.

GENERAL ADVANTAGES OF A STATE BANK.

The outline of the proposed Bank's functions and of its draft constitution is now complete. A number of the advantages which are claimed for it have been developed in passing. It will be useful to summarise these, and to dwell on certain other points, not less important, which do not so naturally arise when it is the Bank's constitution which is the matter in hand.

There are first of all the direct advantages to Government. These affect questions which have been the special business of the Commission. The chief of them may be enumerated:—

(i) The existing "Independent Treasury System," by which, whenever the Government balances are swollen, deliberately or not, large sums are taken off the Money Market, is done away with by the removal of the cause of this system, namely, the absence of a large public or semi-public institution with which large balances could be safely and properly deposited, together with the difficulty of employing Civil Servants in a policy of discretionary loans out of the balances.

(ii) The objections to holding large sums at loan for short periods in the London Money Market are avoided by the method of dealing with sterling resources proposed in Part VI.

(iii) A Bank, responsible for the management of the note issue, has greater opportunities than are open to Government for pushing the circulation of notes and for popularising them by an increase in the facilities available for convertibility.

(iv) The responsibility of Government officials for a variety of financial and semi-financial business is greatly reduced by handing over to a Bank all questions of balances, note issue, remittance, and loans on the London Market.

(v) The Government has at its command the services of officers of the highest position, trained in financial and banking business, instead of Civil Servants who, however full of adaptability and intelligence, have been selected and trained mainly for other purposes.

(vi) A buffer is placed between the Secretary of State and vexatious criticism on small details of financial business.

Next come the immediate advantages to the business world:—

(i) In addition to the partial release of Government balances through their deposit in a central institution, a consi-

derable amount of funds is made available by the reform of the note issue.

(ii) The present wide fluctuations of the bank rate and its normal high level in the busy season may be somewhat moderated.

(iii) The increase of branches, which the union of Government and banking business should promote, would gradually bring sound banking facilities to many parts of India, where they are now almost entirely wanting, both directly and by supplying a basis, in reliance on which private and co-operative banking could be built up.

(iv) The introduction of re-discount facilities, while probably not of the first importance in the immediate future, might greatly aid the eventual development of Indian banking on the most desirable lines which European experience has so far evolved.

At this point something may be said about the bank rate question, and the possibility of obtaining substantially the same results without the interposition of a State Bank.

India suffers not from a high *average* bank rate, but from a wide range of fluctuation and a high *maximum* bank rate. If the *average* bank rate were high, this would mean that the normal return to capital under conditions of least risk was high; and this could not possibly be cured by any monetary device. But a high temporary bank rate, due to the increased volume of cash temporarily required for moving the crops, ought to be capable of amelioration by introducing an elasticity into the credit currency. It is important, however, not to underestimate the magnitude of the problem. Several witnesses have maintained that a loan of three crores made by the Government from its balances or from the Paper Currency Reserve would be a sufficient cure for high bank-rates. I am convinced that this is a serious misapprehension of the facts. What is true is that at any moment an unexpected and sudden loan of three crores by the Government would break the current bank rate. If borrowers and lenders had adjusted themselves to an expectation of 8 per cent. it would be reasonable to hold that a sudden offer by the Government of three crores would bring the rate down to 6 per cent. or less. But this is not the standpoint from which to consider proposals for permanent policy. What present sources of supply would fail and what new sources of demand would spring up, if there were a reasonable expectation beforehand of borrowing in the busy season at 6 per cent.?* Three crores is a very small

* The rate for money is largely determined by the *fringe* of borrowers and lenders who are specially sensitive to any change of conditions. If, for example, the normal maximum rate for money in India was to fall, some up-country traders could afford to pay the cultivator a little more and might hold the goods a little longer, since they would not be forced by high rates for money to hurry the goods foward to a place where they could form a basis for sterling credit.

percentage of the present transactions; it is not $1\frac{1}{2}$ per cent. of the value of the exports; it is barely half of the normal *annual* addition to India's banking resources; and to expect great consequences from the loan of it is to take a short-sighted and superficial view of the causes which really determine the value of money. The proposals made above in regard to a fiduciary issue of notes would have a more substantial effect; but I think it would be optimistic to expect even from them a normal maximum of 6 per cent. Their eventual efficacy is largely bound up with the future development of the use of notes.

This leads us to compare proposals, contingent on the establishment of a State Bank, with proposals for the loan of Government funds to the existing Presidency Banks. If the loans contemplated are comparatively small, there need be no difficulty in lending them on the security of Government paper, and the problem of the terms on which they should be lent, while not quite easy of solution, ought not to prove insuperable. But small loans could not, of course, have large consequences. Though they would, *pro tanto*, be useful and employ funds which are now wastefully idle, to offer them as a cure of high bank rate or of the existing faults in the Indian financial system is to trifle with the problem. If, on the other hand, fairly *large* loans are contemplated, other objections rise to importance. It is uncertain (for reasons given in Section V) whether Government paper would be forthcoming in large quantities as security for temporary loans, and even more uncertain whether it is desirable to encourage the holding of a large amount of Government paper in this way. The Government could only get their funds back as a lender, by spoiling their market as a borrower. Yet there are great difficulties in lending by a Government department against the really desirable security, namely, trade bills. It would take them to a wholly unfamiliar region, and require them to exercise an unaccustomed discretion.

The most serious objection still remains. It would be a perilous policy for the Government to lend on a scale sufficient to influence the bank rate, and for it to remain nevertheless wholly without responsibility for the bank rate policy. The ultimate lender and the ultimate controller of the credit currency cannot safely remain aloof from the control of the bank rate. So long as the Government do not lend and there is virtually no credit currency, the Government can maintain this aloofness from banking. As I have said already, existing arrangements are deeply conditioned by the fact of this aloofness. But if the Government are to lend their balances and to introduce, under their own control and discretion, a proper elasticity into the credit currency, and if they are to do these things on a sufficient scale to make any real difference, then they cannot ignore considerations of bank-rate policy. Such a scheme involves an exercise of judgment on the part of Government officials in high matters of banking policy, without these officials having access to any first-hand banking experience. The Government is driven, therefore, to call in the

assistance of a State Bank to do these things for them and to be responsible at the same time for the bank rate.

These considerations were apprehended by the Government of India when they put forward proposals for a Central Bank in 1900. After mentioning the suggestion of a note issue on the German model, they add:—" Theoretically we admit that the system might be grafted upon the present management of the paper currency by Government. But a Bank would be able to measure the need and extent of accommodation much better than a Government could hope to do, and we believe that in all countries where it has been adopted, the agency of a Bank has been chosen for working this system. Moreover, in India recourse in any form to a currency reserve in the hands of Government would encourage the tendency to look to and rely upon Government exclusively. From this point of view there would be particular objections to applying the system to the currency reserve while it remained under Government control." The last point seems to be a very sound one. Whenever the bank rate was high, there would be a clamour that the Government were not lending all they might.

Proposals for direct loans to the Presidency Banks, on a very moderate scale, from the Government balances and the Paper Currency Reserve may serve to meet certain of the more superficial criticisms. The Government will have an answer to the charge that they keep their whole surplus in a barren form. Indeed, so far, the proposals are good; and for every reason they will commend themselves to the lovers of appearance. But as an attempt to solve the real problems of the Indian financial situation, I do not think they are to be regarded seriously. They are incapable of future development; since they depend for their justification on the trifling and innocuous character of their consequences. And they are right off the line of banking evolution. They do nothing towards extending to India the advantages of civilised experience.

Something has been said of the advantages of a State Bank to the Government and of its direct advantages to the commercial world. I will turn in conclusion to some wider and more general issues; but must treat them briefly.

I attach great importance to the increased stability which a State Bank would introduce into the Indian banking system. India is not well placed at present to meet a banking crisis. The Presidency Banks are already Banker's Banks to an important extent, but they are not strong enough to support the whole burden. In effect the Government keeps a part of the banking reserves, but there is no machinery for bringing its reserves into normal connection with banking. With no central reserve, no elasticity of credit currency, hardly a re-discount market, and hardly a bank rate policy, with the growth of small and daring banks, great increase of deposits and a community unhabituated to banking and ready at the least alarm to revert to hoarding, even where it had been seemingly abandoned, there are to be found most elements of weakness and few elements of strength.

A recent article by Mr. H. M. Ross in "Capital" (September 4th, 1913) brings out these points very plainly. This article contains much which deserves reference, but the following passage is, in the present connection, the most important:—

"India and the United States of America are now practically alone among the great trading countries of the world in possessing no Central Bank. In view of the American banking crisis of 1907 the relation is an ominous one. The vast monetary resources of the United States, badly handled and selfishly hoarded when they should have been freely used where most required through the medium of a great central institution, were of no avail to avert wholesale bankruptcy and a general suspension of payment by the Banks. In a similar crisis it would be the policy, nay, it would be the duty of each Presidency Bank to conserve its resources for the benefit of its particular area. In the general interests of the country this should not be." Mr. Ross might have added that India and the United States are also alone in having no re-discount market, no elasticity in the note issue, no bank rate policy, and an "Independent Treasury System" in place of a Government banker. In America the 1907 crisis served to demonstrate that such a system is indefensible, and the country is now engaged in remedying these defects so far as is possible in the very difficult circumstances which arise out of the presence of innumerable small Banks, on the one hand, all with vested interests and a terror of anything which might conceivably diminish their profits, and of a public, deeply suspicious of all moneyed interests and of anything which might strengthen their power, on the other.* In India the obstacles are far less to the introduction of the recognised preventives for the diseases of the financial body.

I have already pointed out the importance of a strong central institution in relation to the development on sound lines of native Joint Stock Banks. The encouragement of re-discount should be an encouragement to these Banks to use their funds, as they ought, in the assistance of trade, instead of in speculation or in fixed enterprises.

The great increase of branches in country districts may lead to the State Bank's playing an important part in the development of

* Since the above was written, a new Currency Law for the United States has been carried. It is interesting to notice that, while decentralisation is secured by the establishment of from 8 to 12 regional banks, the cohesion and strength of the new system will depend on the central Federal Board to be established at Washington (not New York). This Federal Board seems from the available account to have some slight analogy with the Central Board for India proposed above. "The Federal Board will consist of the Secretary of the Treasury, the Comptroller of the Currency, and five members appointed by the President with the consent of the Senate. Its powers are enormous. A vote of five of its members can require a regional bank to discount the paper of other regional banks. It can fix the rate of discount. It can temporarily suspend the reserve requirement. It can honour or refuse requests for notes from the regional banks and has other important supervisory functions." The Government will bank with the new regional banks, and a principal object of the new organisation is to encourage the practice of re-discount.

co-operative banking amongst agriculturists. The local branches should always aim at being the Co-operative Bank's bank and at helping them by judicious loans.

This increase of branches will be much facilitated when a single institution is in control of banking, the Government's balances, and the currency chest in country districts. At present there is apt to be unprofitable discussion between Government and Presidency Banks about (*e.g.*) the interest payable on loans or the subsidy required to support a branch bank where there is now a District Treasury. It would pay Government to give any subsidy short of the expense of maintaining the Treasury. But they are naturally unwilling to hand over too much profit to private persons and yet are not in a good position to gauge how much this profit would be. So long also as the District Currency Chests are not handed over to the branch bank, some economies are open to the Government Treasury which are not open to the bank. A system of haggling between the Government and Presidency Banks as to the opening of branches, in which both parties have to be convinced that they are certainly making a good bargain, must be worse than one in which the interests of the two parties are joint instead of opposed and the only consideration is whether a branch is worth opening *on the whole*.

In conclusion it is worth while to recall the Government of India's latest pronouncement on the subject, when in June, 1901, they were "regretfully compelled" to "hold the scheme in abeyance":—"We desire at the same time to record our deliberate opinion that it would be distinctly advisable, if practicable, to establish a Central Bank in India, so as to relieve Government of its present heavy responsibilities and to secure the advantages arising from the control of the banking system of a country by a solid and powerful Central Institution."

IX.

SOME ADVERSE CRITICISMS.

The chief criticisms of proposals for a State Bank which I remember to have heard are the following:—

(1) That there is no popular clamour for it.

(2) That it would increase the responsibilities of the Secretary of State and expose him to vexatious questions in Parliament.

(3) That India is too large and too various in local custom to be worked by a single Bank.

(4) That the local jealousies of Bombay and Calcutta are too strong.

(5) That the former Bank of Bombay suspended payment in 1866.

(6) That talent is not available in India to staff the Bank's directorate.

(7) That it would not be fair on the Exchange Banks.

It is not quite just to these criticisms to give so bare a catalogue of them. Some of them become more imposing, when they are enlarged on. In regard to several it is possible for each individual to judge for himself how much weight ought to be given them. An admirable summary of the views expressed by witnesses can be gathered from pages 18, 19, and 20 of the Index to the evidence.

(2), (3), (4) and (6) are, in my own opinion, the more substantial. With (2) I have already dealt. The particular constitution proposed for the Bank is designed, in part, to mitigate the force of objections (3), (4) and 6. Of these (3) has, I think, very little force provided that reasonable autonomy is allowed to the local Boards. I pressed all the witnesses, who raised this objection to particularise the difficulties, arising out of the size and variety of India, which they chiefly had in mind; but without success. With regard to (6) it must not be forgotten that at least as much talent will be available as at present.

The "vested interests" question is turning out much less serious than might have been expected. The Presidency Banks of Bengal, Bombay and Madras show no pronounced signs of hostility, and the authorities of the two latter have declared themselves, subject to certain conditions, definitely favourable. The present system is so wasteful that a change will provide a wide margin of profit for the shareholders of these Banks to participate in.

The Exchange Banks seem likely to oppose any substantial change in the present position. Their legitimate trading interests, however, are very fully safeguarded in the above proposals; and, as they will share in the advantage of increased stability in the Indian financial system, opposition will probably be mistaken even in their own interests. They will be but repeating the mistake which they made in 1892 in opposing the closure of the mints. It might have been expected that they would have welcomed a measure intended to introduce stability into their business, and which has in fact made the fortunes of all of them. But they held at that time that it was on the fluctuations of exchange and on the supposed bounty given to exports by a depreciating currency that they chiefly depended for their profits.

In 1900-01 the amount of consideration which should be paid to the exclusive claims of the Exchange Banks was the subject of some difference of opinion between the Government of India and the Secretary of State. The former wrote:—"We cannot see that the Exchange Banks make out a strong claim for protection, and a suggestion which has been made that a Central Bank should be bound to make any and all remittances through their agency is out of the question." And, later, in answer to the Exchange Banks' protest against "State-aided Competition":—"We could have wished that this contention of the Banks, which appears to us to

be untenable, had been supported by some clearer indication of the actual manner in which the competition they deprecate may be expected to prove unfair and injurious." This comment is equally applicable to the evidence given to ourselves by Mr. Toomey and Mr. Fraser. As arising out of this evidence, it may be pointed out that the Exchange Banks have absolutely unrestricted opportunities for purely Indian business that this side of their activities has very greatly increased, and that Mr. Toomey deliberately depreciated the importance to them of the business of attracting deposits in London for use in India, a part of their business on which they used greatly to pride themselves and which was at one time no small part of the ground on which they claimed special consideration.

The memory of the business world is short. Apart from vested interest, the main difficulty in the way of the above proposals is the great *vis inertiæ*, engendered by an experience of good times and only to be dispelled, perhaps, by a taste of trouble. Further, I do not believe that reasonable opposition to them will chiefly depend upon the kind of detailed criticisms enumerated above, or that their essential parts are open to specific attack. The real ground of objection is at the same time more vague and better founded. The proposed scheme is a large one, and all of its consequences cannot possibly be predicted with certainty. Such a scheme must naturally provoke a doubt as to whether it is worth while to embark for a *terra incognita* which may, for all one knows, contain something hazardous in it. But the land must not be thought more unknown than it really is. The above proposals contain nothing more than an adaptation to Indian conditions of methods which have been tried successfully in a great many places.

6th October 1913. J. M. KEYNES.

APPENDIX A.

THE RELATION OF STATE BANKS TO THEIR GOVERNMENTS.

The existing arrangements in various continental countries and in Japan are given below in outline. I describe the Reichsbank and the Bank of France in a certain amount of detail, and the rest very briefly indeed. because these two are the prototypes of several others, the constitutions of which contain few original ideas.

Reichsbank.

No part of the capital is owned by the State.*

The authorities of the Bank are:—

1. The *Bank-Kuratorium*, consisting of the Imperial Chancellor as Chairman and four members, one appointed by the Emperor and three by the

*When in 1876 the Bank of Prussia was converted into the Reichsbank, the Capital previously held by the Prussian Government was repaid.

Bundesrat. This is of the nature of a Board of Trustees and meets only four times a year to receive a general account of the Bank's operations.

2. The *Bank-Direktorium*, consisting at present of a President, Vice-President and six members, all appointed for life by the Emperor on the nomination of the Bundesrat. This Board (to quote the Bank Act) is " the managing and executive authority of the Reichsbank . . . . . Its orders are to be sanctioned by a majority vote, and subjected to the instructions and directions of the Imperial Chancellor."

The *Direktorium* is "endowed with special independent powers, even though these can be checked by higher officials; it acts in its own name as the central managing body of the Reichsbank, forms its resolutions on its own responsibility by majority vote, and has the rights of a 'supreme imperial board.' "*

3. The Central Committee of Shareholders (*Zentralausschuss*) consisting of 15 members elected by the general meeting of shareholders. This committee must meet at least once a month. Reports must be presened to them, relating to most of the more important weekly items in the Bank's transactions, and containing a statement of the *Direktorium's* views as to general policy. The committee's powers are purely advisory.† But the Bank Act enumerates a number of questions in regard to which " the suggestions of the Central Committee should receive special consideration." Amongst these may be mentioned the filling up of vacancies in the *Direktorium;* the drawing up of the annual balance sheet; the maximum amount to be loaned by the Bank in advances against collateral; the discount rate and the loan interest rate, as well as changes in the principles and the terms on which credit is to be given. The interests of the shareholders are further safeguarded by the annual appointment by the Central Committee of three of their number as deputies having the right to attend with advisory powers all sittings of the *Direktorium* and to examine the books of the Bank.

The salaries and pensions of the members of the *Direktorium* are fixed annually in the Imperial Budget.

The ordinary officials of the Reichsbank " have the rights and duties of Imperial functionaries," and are precluded from holding shares in the Bank.

The members of the Central Committee of Shareholders draw no stipend.

The rules governing the management of the Local Head Offices (*Reichsbank Hauptstelle*) also deserve notice. The Reichsbank now has 486 branches‡ (as compared with 569 of the Bank of France), of which 20 are Head Offices. Each of these offices is under the supervision of a local board of at least two members of a Commissioner (*Bank-Kommissarius*) appointed by the Emperor. The executive authority is in the hands of two managing officials. There is also for each such office a district committee, appointed by the Imperial Chancellor from amongst the shareholders of the Bank resident in the city where the Local Head Office is located. The powers of the local committee are similar to those of the Central Committee, and they also have the right to appoint two or three deputies for purposes of closer supervision.

These Local Head Offices have a high degree of independence. They are empowered to carry on independently in the district assigned to them by the *Direktorium* all forms of transactions permitted by the Bank Act. The signatures of the two managing officials of a Local Head Office are legally binding on the Reichsbank.

Besides the 20 Head Offices, there are 77 offices which have nearly as much independence as the Head Offices. All the rest of the branches are sub-offices directly dependent on offices or Head Offices, and requiring approval for their transactions by the higher office. According to the strict rule " no bill may be purchased by them which has not been previously laid before the higher office." But this rule has gradually been mitigated so that the higher branch can name to the sub-office those persons and business houses from whom, without inquiry in each case, bills may be purchased

* *See* the official history of the Reichsbank, 1876-1900.

† Except on one or two minor points, not deserving of reference here, in regard to which they can veto change.

‡ It originally opened in 1876 with 201 branches.

within the fixed limits of credit, with the reservation, however, that sanction may subsequently be refused.* In other respects the powers of sub-offices have been gradually developed. The chief obstacles according to the official history, which have retarded the free development of sub-offices, are especially relevant to Indian conditions. In the first place the keeping of large balances at the sub-offices, or alternatively the too frequent remittance of money backwards and forwards, would have been involved. Sub-offices have not been allowed, therefore, on their own authority to accept fixed deposits on the one hand or to make advances against collateral on the other. In the second place "at the creation of the Reichsbank most of the directors of sub-offices were not officials trained in banking, but agents some of whom performed the duties of the office only as incidental work and recieved for it no fixed salary, but only a percentage of the profits." In the course of its development the Reichsbank has tried two different lines of advance, the grant of increased powers to sub-offices in places where the amount of business was important, and the transformation of such sub-offices into offices. On the whole the second line of advance seems to have been the more successful.

Bank of France.

No part of the capital is owned by the State.

The authorities of the Bank are:—

The Governor.

Two Deputy Governors.

A General Council (*Conseil Général*) of 15 *Régents* and 3 *Censeurs*.

The Governor and Deputy Governors have always (since 1806) been appointed and removable at will by the Minister of Finance. The *Régents* and *Censeurs* are appointed by the 200 amongst the shareholders who hold the largest number of shares.† Three of the *Régents* must be treasury disbursing agents (*Trésorier-Payeurs Général*), *i.e.*, officials, and five must come from the business portion of the shareholders, from amongst whom the *Censeurs* also must be chosen. The *Censeurs* are inspectors or auditors. They attend meeting of the *Conseil Général*, have access to the records of the Bank, and are entrusted with the duty of reporting any irregularities to the shareholders.

The *Régents* and *Censeurs* divide themselves up into five committees to deal with special departments, *e.g.*, the *Comité d'escompte*, the *Comité des billets*, *etc.*

The Managers of the Branches are appointed by the Minister of Finance from amongst three candidates nominated by the Governor of the Bank, who has also the power of dismissal. The names are considered, as well, by the *Conseil Général*.

It will be noticed that, so far as the letter of the law goes, the power of the representatives of the shareholders is very much greater than is the case with the Reichsbank. This is much modified, in practice, by the following considerations. In the first place the Governor has the right of veto. This right, though the occasions of its use in the last hundred years have been very rare indeed, preserves the ultimate authority of the State over changes in policy or regulation unimpaired. In the second place the official element on the *Conseil Général*, made up of the Governor, the two Deputy Governors and the three *Trésorier-Payeurs Général* amongst the *Régents*, commands six votes out of a total of 18. Since the Governor has a casting vote, if only three of the 12 unofficial members vote with the officials, the latter have an assured majority. The practical effect of this has been, in the words of M. Rouland who was Governor in 1865, that "nothing of any description which concerns the great interest of the public, or the larger duties which the Bank has to perform towards commerce and industry, is left to the discretion of what is called the interested party (*i.e.*, the shareholders)."

* *See* Official History of the Reichsbank.

† This provision is quite peculiar to the Bank of France. A shareholder has at present to hold at .£t 20,000*l*. worth in order to participate.

The Imperial Bank of Russia.

This Bank stands by itself (so far as the larger countries are concerned) in being wholly owned, as well as managed, by the Government. It is under the direct control of the Minister of Finance.

*The Bank of Belgium.**

No part of the capital is owned by the State.

The Governor is appointed by the King for five years, and may be reappointed. The active administrative council consists of the Governor and six directors appointed by the shareholders. The shareholders also elect a council of seven censors to audit and supervise. The Government exercises further supervision through a Special Commissioner, and Article XXIV of the Bank Act runs:—"The Government has the right to control all operations. It shall have the power to prevent the execution of any measure which shall be contrary to the law, to the statutes, or to the interests of the State.

The Bank of the Netherlands.

Closely similar to the Bank of Belgium.

The Austro-Hungarian Bank.

No part of the capital is owned by the State.

The Governor and two Deputy Governors of the Bank are appointed by the State.

The Bank of Italy.

The capital is privately owned, but the nomination of the Director-General must be approved by the Government; and the Ministers of Agriculture, Commerce, and the Treasury form a board with powers of supervision and inspection.

The Bank of Spain.

This is a private institution, but privileged and standing in very close relations to the Government.

The Bank of Japan.

Baron Sakatami, ex-Minister of Finance, writes as follows:—"When the Bank was first established, the Government was a very large shareholder, but these shares were afterwards transferred to the Imperial Household Department . . . . . The Government's supervision is very strict. It appoints the Governor and the Deputy Governor; the directors are also appointed by the Government from among candidates elected by the shareholders; the Government appoints official inspectors from among the officials of the Department of Finance . . . . ."

APPENDIX B.

State Banks and Private Capital.

On the occasion of the last renewal of the Reichsbank Charter in 1909, many people urged that the private shareholders ought to be bought out by the Government on the avowed ground that these were making profits which ought to accrue to the State. The following quotation from an article

*See *The National Bank of Belgium*, by Charles A. Conant.

written by Professor Lexis in the course of this controversy is instructive:—"The officials of a pure State Bank have merely to adapt themselves to the regulations coming to them from above; but a Bank of issue with private capital, even when entirely managed by the State, has a sort of independence as regards the State—an independence which protects it against interference with the vital conditions of its existence. For the former, indeed, the interference of legislation is always needed; but the latter must never forget that a great private capital is in its charge. The Central Committee of the Reichsbank has undoubtedly only a very moderate authority, but its influence, nevertheless, is far greater than that of the advisory board of a State railroad company, because it represents the owners of the bank capital."

It was noticeable that the demand for the suppression of the private capital of the Reichsbank came, not from the Socialists, but from the Agrarians. "The Agrarians," it has been said, "wish to render the State master of the Bank, because they are to-day masters of the State. If the State becomes master of the Bank of the Empire, the Agrarians hope that nothing can any longer prevent them from compelling the State to employ the funds of the Bank in the execution of their programme."

There was a similar controversy in Belgium in 1900. The following arguments against the abolition of private capital may be quoted from the *Documents Parliamentaires** :—"There is, first, the confusion of public and private credit, to the great damage of each; for they ought to remain distinct, for their respective good and for the mutual assistance which they are at times called upon to lend to each other. Further, there is the acceptance by the State of a task—the task of discounting—which is not within its competence, and of which, even with the best of will, it will acquit itself badly. It is neither wise nor practicable to suppress the legitimate stimulus of private interest in such affairs as discount. It must not be believed that in such a matter disinterestedness alone suffices or can afford a better guide than the foresight of those who run the risks and reap the benefits of such operations."

APPENDIX C.

The Division of the Profits of the Reichsbank.

The duties to be performed by the Reichsbank without remuneration and the rules governing the proportion of the profits which accrues to the shareholders are as follows:—

(1) The Reichsbank must purchase gold bullion tendered to it at a fixed rate. It is "required to accept payments for the account of the Empire and to make disbursements without compensation." It bears the whole expense of management of the note issue.

(2) The Reichsbank must pay a tax of 5 per cent. to the Government on the excess of the fiduciary issue beyond a certain amount.

(3) "The net annual profit of the Reichsbank is to be divided at the close of each year in the following manner:—

"1. In the first place, a regular dividend of 3½ per cent. of the capital is to be distributed among the shareholders.

"2. Of the remainder, 10 per cent. is to be transferred to the reserve fund, 20 per cent. to the shareholders, and 70 per cent. to the Imperial Treasury.

"3. If the net earnings are less than 3½ per cent. of the capital, the difference is to be made up from the reserve fund."

These arrangements, however, have been altered at every decennial revision of the Bank Act. Originally (1875) the guaranteed dividend was 4½ per

*See Conant, *History of the National Bank of Belgium.*

cent. (instead of 3½ per cent.), 20 per cent. of the balance went to reserve, and of the rest the State took a quarter when the total dividends of the shareholders exceeded 8 per cent. In 1891 3½ per cent. was substituted for 4½ per cent., and the one-fourth share began to accrue to the State when the shareholders' total dividend exceeded 6 per cent. After 1901 the share of the State began as soon as the 3½ per cent. dividend and the transfer to reserve had been made, and the shareholders received 25 per cent. of the surplus. The present arrangement dates from 1911.

The actual dividends of the shareholders in recent years have averaged about 7 per cent.:—

	Per cent.
1907	9·89
1908	7·77
1909	5·83
1910	6·48
1911	5·86
1912	6·95

In 1912 the State received 1,088,732*l*. as its share of profits and 231,374*l*. as note tax 1,320,106*l*. altogether; as compared with 879,881*l*. in 1911, 1,001,139*l*. in 1910, 822,409*l*. in 1909, and 1,280,838*l*. in 1907.

The agreement between the shareholders and the State is subject to revision every ten years. And, further, "the Empire reserves the right of option on January 1, 1891, and thereafter at the expiration of every ten-year period: (*a*) of discontinuing the Reichsbank established by this Act, and acquiring its property on the basis of the book values, or (*b*) of acquiring the total stock of the Reichsbank at valuation . . . . In either case the reserve fund, in so far as it is not required to defray losses, is to be equally divided between the shareholders of the Empire."

If at any of the decennial periods the Government had taken full advantage of this provision, it would have been much more disadvantageous to the shareholders than the new arrangements for division of profits actually made.

Note by Sir James Begbie.

I have signed the Report subject to the following note:—

1. I regret that I am unable to concur in the conclusions and recommendations contained in the Report on the subject of the currency policy.

2. That policy has been directed to the attainment of stability in the exchange value of the rupee by means of gold reserves collected from the profits realised on the coinage of rupees. Whilst it has been successful in achieving that object, it has brought into existence an extensive token currency which, in my opinion, is not conducive to the interests of India. I regard that form of currency as undesirable for a country which absorbs gold on a very large scale.

3. A brief examination of some of the chief arguments brought forward in favour of the measures actually adopted for securing stability in the exchange value of the rupee, and of those urged against the use of the means originally proposed for securing stability, *viz.*, a gold currency with gold in active circulation, may help to make my point of view clear.

4. I take first the arguments given in support of the existing policy. The point has been pressed that the public preferred and demanded rupees, and the demand had to be met. That is a reason which carried considerable weight in the early years of the period during which the policy has been developed, but it has now lost its force. The public have absorbed during the last 12 years approximately equal amounts of rupees and sovereigns, but the demand for sovereigns has rapidly increased during the last four years. These recent gold requirements show an important change in the currency needs of the people and indicate a preference for gold over rupees.

5. The next argument is one which has latterly come into prominence, *viz.*, that the Indian system has close affinities with the currency systems of certain other countries. Such analogies are, I consider, unsafe as a guide to Indian policy, because the conditions are not identical. In none of those other countries is there the same private absorption of gold that there is in India. Whatever experience elsewhere may be, the recent demands for gold in India show a loss of confidence on the part of the public in the token rupee, and that is a situation that should not be ignored. The need for confidence to secure the exchange value of the rupee is recognised, but not the need for confidence in the currency in other respects. It is no longer possible to say that the token rupee is preferred by the Indian public and satisfies their currency requirements in face of the fact that they have latterly exhibited so strong a desire for gold as the statistics indicate. At least there is not now such general confidence in the rupee as would, in my opinion, alone warrant further large extensions of the token currency.

6. Another argument given is that it is desirable to educate people in the use of more economical forms of currency than gold. That, of course, is a desirable object, but the experience so far gained does not inspire the hope that the educative effect of present methods will be successful in attaining it. The increased circulation of notes may be pointed to as an advance towards the use of more economical forms of currency; but it is due, not solely to a desire to economise in currency, but partly at least to increased facilities for the employment of notes. Against this favourable sign must be set the increased absorption of sovereigns. This demand for gold coin, accompanied as it has been by increased demands for gold bullion, dominates the whole currency situation. For a country which takes gold in great quantities an extensive token currency is most unsuitable. It has the usual effect of driving gold out of circulation. It has the still greater disadvantage that it keeps the gold out of useful employment. People who value gold so highly as to store and hold it to the extent witnessed in India are not likely to invest or make other profitable use of it, so long as they have to take the risk of being repaid in token coins when they realise their investments. The token cur-

rency not only prevents the holders of the gold from utilising it to some advantage, but the country as a whole loses the benefit that should accrue to it from the possession of great wealth. While, therefore, the process of education in the use of economical forms of currency is proceeding, the probabilities are that the people will none the less continue to amass their growing wealth in solid gold. In my opinion, what is needed is not education in the use of economical currency so much as education in the use of the stored up gold. The first step, however, is to convince the people that if they use their gold they will get it back when they want it, and that cannot be done while there is this extensive and expanding token currency. A currency in which gold was a more prominent feature and to which token coins were less freely added would be more practical as an educative force. Gold coins would be suitable and convenient for many ordinary currency purposes, and by using them the public would be gradually led to use gold for other purposes, such as investments, especially if a considerable circulation of gold existed, sufficient to inspire the public with confidence that when they wanted their gold restored to them they could get it.

7. I come next to reasons advanced against a gold circulation. It has been said that gold in reserves is better than gold in circulation for the support of exchange. That, of course, is true, but it is equally true that gold in circulation is a better protection for exchange than token coins. Gold in circulation can never endanger exchange stability. It cannot be too strongly emphasised that danger lies in the token currency alone when unfavourable trade conditions prevail. In the words of the Report (paragraph 62), "It is the surplus tokens and not the gold which will seek an outlet at times of weak exchange." Moreover, reserves of gold can be accumulated from a gold circulation through the note issue and a good banking organisation. Even under the existing system the most satisfactory part of the gold reserves is the gold in the Paper Currency Department. The full equivalent of the currency issued against it is saved in gold for the reserve, whereas the Gold Standard Reserve represents only about one third of the token currency from which it was saved, and will redeem only that proportion of it, unless the extreme step is taken of melting down rupees. Also, a considerable portion of the coin reserve of the Note Department must be held in rupees at present. With a free circulation of gold a much smaller portion could be held in rupees and a correspondingly larger part in gold.

8. The objection that gold is an expensive form of currency is one which, I consider, can easily be pressed too far in the case of India. The token currency is being steadily exchanged for gold. To the extent at least to which that process is carried the country is not saved the expense of the gold by the present system. Also, if, as I think is the case, the token currency has the effect of encouraging and strengthening the hoarding habit, it is not true economy to object to the expense of a gold currency, and as a

result to force gold out of circulation and prevent its employment in other useful ways, thus causing extreme waste.

9. Another objection is that gold coins, especially coins of small value, would be formidable rivals to currency notes. In my opinion notes will usually be preferred to coin—whether gold or silver —for such purposes as bank cash reserves and frequently for effecting remittances. If the use of notes for other purposes is endangered in any way by a circulation of gold coins because the latter are preferred, it has to be remembered that notes may be affected by the growing demands for gold. The possibility that these demands will spread should be recognised. If the public want gold they will get it whether they hold notes or rupees, and when they prefer gold they are not likely to be satisfied with notes, payment of which can be demanded only in rupees.

10. The hoarding habit in India is no doubt a difficult problem. Its recent rapid development in increased demands for gold, and the possibility of its further expansion, make it a question of the highest importance. I do not, however, think the opinion expressed in paragraph 75 of the Report that "the hoarding habit is sanctioned by the experience of centuries in India and by religious and racial laws and customs" sufficiently accounts for the accelerated pace it has latterly acquired. In my opinion, that is to a large extent the outcome of the policy which has brought into existence the extensive token currency. Up to the closing of the Mints in 1893 to the free coinage of silver the public had been accustomed for generations to full value coins for their currency requirements, and they are not now prepared to hold their profits and savings in the form of overvalued rupees. Hence their preference for gold, both coin and bullion. I am therefore unable to agree that the habit is one which should be regarded as inevitable in Indian social or religious conditions and not susceptible to treatment. The statistics show that great progress has been made in attracting the cash reserves of the people into useful and profitable channels, such as investments and deposits with banks. But they also show this later reversion to hoarding on an extended scale, which is thus a retrograde movement, indicating a greater and not unnatural desire for solid security than for profitable returns on investments in a currency medium which does not provide the kind of security now clearly preferred. It seems to me that it is not to the interest of India to have its rapidly accumulating wealth diverted into idle hoards by the token currency policy.

11. But even if that policy has not been the cause of the increased demand for gold, the difficulty remains of drawing hoarded gold into profitable use. Capital is proverbially timid and nowhere more so than in India. If, therefore, the gold held in India is to be attracted into useful employment it can, I think, be done only by providing security that when it is invested the investments will continue to represent gold, and be convertible into gold, by means of a gold currency policy in which the public will have confidence.

12. For the reasons I have indicated, I am of opinion that the true line of advance for the currency policy is to discourage an extension of the token currency by providing increased facilities for the distribution of gold when further increases in the currency become necessary. These greater facilities should, I consider, include the issue of gold coins from an Indian mint of a value more suitable for general currency use than the sovereign and half-sovereign, for the purpose of assisting the distribution of gold when, as is frequently the case, the balance of trade is strong in India's favour and gold arrives in considerable quantities. I also think that supplies of gold coins should be laid down in the up-country districts with the object of giving the general public effective opportunities of obtaining gold coins.

13. I do not, however, recommend the dispersal into circulation of any of the existing gold reserves. The maintenance of the exchange value of the rupee should continue to be the guiding principle of the policy, and the reserve accumulated specially to secure the stability of exchange should continue to be specifically set apart for that purpose. But as future additions to the currency become necessary by reason of favourable trade balances, the additions should take the form of gold which will be imported in settlement of the balance of trade. With the present system it is sometimes found necessary to anticipate fresh additions to the currency by providing silver for coinage from the reserves. In my opinion it would be better to issue gold from the Paper Currency Reserve to the public in such circumstances and allow the gold when imported later to accumulate again in that reserve.

14. The procedure which I have suggested would, of course, be applicable only to normal times. Should the situation caused by the crisis of 1907-08 recur, and the gold reserves be depleted to support exchange and the silver reserves inflated, the issue of gold for internal purposes would require to be suspended until the surplus rupee reserves were reabsorbed by the public and the gold reserves restored. So long as such an extensive token coinage is in existence, it is important that the public should use it.

15. I also regret to be unable to assent to the proposals contained in the Report whereby the Treasury balances in India and in London may be utilised for the purpose of maintaining the exchange value of the rupee, and for the provision of fresh supplies of coined rupees. I see no good reason for associating the Government cash balances with currency reserves for purely currency purposes. If the gold reserves should not be strong enough to maintain exchange in a time of difficulty, it would be better to raise additional funds by the issue of temporary loans than to rely upon cash balances for such a purpose.

16. Also, I consider the cash balances an unsuitable source from which to provide supplies of silver for coinage. For example, the balances laid down in London represent mainly the proceeds of Council drafts which are sold throughout the year at current rates

of exchange, and frequently at rates well below gold import point. If money so provided in London is used to add rupees to the currency in India it means that fresh rupees are issued at more than the established ratio of 15 rupees to the sovereign.

17. The same objection applies to sales of Council drafts below gold point against the Gold Standard Reserve in India for the re-issue of rupees withdrawn from circulation to support exchange, as in 1909-10, and against that Reserve and the Paper Currency Reserve for the provision of new currency. The necessity for working at gold import point in such circumstances does not appear to be sufficiently recognised, but in my opinion it is most important. To work the system by means of drafts at any other rate not only breaks the standard ratio, but lays Government open to the charge of departing from the standard to secure the profits on coinage.

18. The system by which the proceeds of all Council drafts sold are passed into the general balances of the Secretary of State, and portions are subsequently allocated to the Gold Standard or Paper Currency Reserves is open to the same objection. It seems necessary to separate sales on account of those latter funds from sales for purely Treasury purposes, as they should be made only at the special rate indicated above.

19. I am not convinced that a good case has been made out for the location of the metallic portion of the Gold Standard Reserve in London. I consider that the portion which the Commission are recommending to be held in gold should be held in India earmarked for the support of exchange, and that when it has to be used for that purpose, it should be issued to the public who want it for export. I should not, however, be in favour of an immediate transfer of the gold now held in London to India. But when the Reserve in London is again drawn upon for the support of exchange, it should not later be restored to London, but should be allowed to accumulate in India in gold.

20. I also consider that the coin reserve of the Paper Currency Department should be held exclusively in India. It is in India alone that the notes for the redemption of which the Reserve is maintained fall to be converted into coin on demand. The transfer of a portion of the Reserve to London is a measure which is not calculated to improve the credit of the note issue and is therefore undesirable. For the same reason, I am unable to approve of the proposal to employ in London a portion of the Reserve in temporary investments.

J. BEGBIE.

CONTENTS.

Report of Committee on Indian Exchange and Currency, pages 235—296.

Report of Committee on Indian Exchange and Currency, 1919.

To

THE RIGHT HON'BLE EDWIN S. MONTAGU, M.P.,
SECRETARY OF STATE FOR INDIA.

1. Terms of reference.—We were appointed on the 30th May 1919, as a Committee to advise in regard to the future of Indian Exchange and Currency. Our terms of reference were as follows:—

> "To examine the effect of the war on the Indian exchange and currency system and practice, and upon the position of the Indian note-issue, and to consider whether, in the light of this experience and of possible future variations in the price of silver, modifications of system or practice may be required; to make recommendations as to such modifications, and generally as to the policy that should be pursued with a view to meeting the requirements of trade, to maintaining a satisfactory monetary circulation, and to ensuring a stable gold exchange standard."

INTRODUCTORY.

2. Witnesses.—We have held 40 meetings and examined 28 witnesses. We have endeavoured to obtain evidence of as widely representative a character as possible. The official side of the case has been placed before us by Sir Lionel Abrahams, K.C.B., Assistant Under-Secretary of State, Mr. F. H. Lucas, C.B., C.V.O., Financial Secretary at the India Office, and Mr. M. M. S. Gubbay, C.S.I., C.I.E., Controller of Currency in India, who, in addition to serving as a member of our Committee, was the accredited spokesman of the Government of India. Sir W. Meyer, G.C.I.E., K.C.S.I., who was Financial Member of the Governor-General's Council in India for practically the whole period of the war, also gave evidence. In addition, we had the advantage of hearing Sir David Barbour, K.C.S.I., K.C.M.G., who occupied the post of Financial Member of the Governor-General's Council from 1887-93, when the policy of closing the Indian mints to the free coinage of silver was adopted, and subsequently served as a member of the Indian Currency Committee presided over by Sir Henry Fowler (later Lord Wolverhampton) in 1898-99.

In order to ensure that all important representative associations in India should be given the fullest opportunity to nominate

witnesses, we requested the Government of India, through the Secretary of State, to renew the invitation they had issued prior to our first meeting, and to facilitate the deputation of witnesses to this country. The majority of the Chambers of Commerce and other representative associations in India elected to submit their views in writing rather than depute a witness for the purpose. All the memoranda received from them will be found in the volumes of our proceedings, and we need scarcely say that we have given them the careful consideration to which the responsibility and experience of their authors entitle them. Witnesses were specially deputed from India on behalf of the Indian Merchants' Chamber and Bureau, and the Bombay Millowners' Association.

Eight other witnesses representative of financial, commercial, and banking interests in the East appeared before us. Apart from the representatives of the Eastern Exchange Banks Association, these included Lord Inchcape, G.C.M.G., K.C.S.I., K.C.I.E., who served on the Secretary of State's Council from 1897 to 1911; Mr. M. de P. Webb, C.I.E., C.B.E., formerly Chairman of the Karachi Chamber of Commerce; Mr. J. N. Stuart, of the Indian Tea Association; Sir E. Rosling, of the Ceylon Association; Mr. J. F. N. Graham, who represented the Glasgow Chamber of Commerce; and Mr. S. R. Bomanji, Member of the Indian Merchants' Chamber and Bureau, Bombay. Invitations were also issued to the East Indian Section of the London Chamber of Commerce and the Manchester Chamber of Commerce, but these bodies did not consider it necessary to nominate a special witness. The Ceylon Chamber of Commerce also found it impossible to depute a representative to give evidence before us.

3. Prior to our appointment the Secretary of State had appointed Professor C. G. Cullis, D.Sc., and Professor H. C. H. Carpenter, F.R.S., of the Imperial College of Science and Technology, to conduct an enquiry into the conditions of silver production, the prospects of future output, and the causes by which it was likely to be influenced. We were able to avail ourselves of the results of this valuable investigation, and the two gentlemen who had conducted the enquiry appeared before us. Mr. E. L. de M. Mocatta, partner in the firm of Messrs. Mocatta and Goldsmid, bullion brokers, also gave evidence on the conditions and prospects of the silver market.

We found it necessary to examine the bearing of the exchange value of the rupee on the level of prices in India, and in response to our request for evidence on this point, the Government of India deputed Mr. K. L. Datta, who in 1910-13 had conducted an enquiry into the rise of prices in India from 1895, to appear before us, not indeed as the official spokesman of the Government, but as an authority on prices and economic conditions in India. We also took evidence from Sir James Donie, K.C.S.I., a retired officer of the Indian Civil Service, and Mr. James Campbell, O.B.E., I.C.S., on this aspect of the case.

Sir Brien Cokayne, K.B.E., Governor of the Bank of England, gave evidence with reference to the Indian demand for the precious metals.

The remaining witnesses were:—Mr. F. T. Rowlatt, Governor of the National Bank of Egypt; Mr. F. I. Kent, Director of the Foreign Exchange Section of the Federal Reserve Board of the United States of America; Sir Stanley Reed, K.B.E., Editor of the *Times of India*; Mr. J. M. Keynes, C.B., a Member of the Royal Commission on Indian Finance and Currency, 1913-14; Professor H. Stanley Jevons, of Allahabad University; and Mr. S. K. Sarma, a student of Indian currency questions.

We wish to express our sincere regret at the premature death of Sir Lionel Abrahams, K.C.B., Assistant Under Secretary of State for India, and our sense of the loss which the public service has suffered in the death of an officer of unrivalled knowledge and experience in all questions connected with Indian currency and finance. Our records show the high value and wide scope of the evidence which we received from him in the course of our enquiry.

LIMITS OF TERMS OF REFERENCE.

4. Scope of enquiry.—At the outset of our Report we would draw particular attention to the last phrase of our reference under which we are directed to make recommendations with a view "to ensuring a stable gold exchange standard." This precluded us from considering the question of returning to a silver standard such as existed before 1893, or of introducing a bi-metallic standard. We think it well, however, to add that we are unanimously of opinion that no useful end would have been served by an enlargement of our reference so as to permit the consideration of these alternatives.

THE CHAMBERLAIN COMMISSION.

5. Royal Commission on Indian Finance and Currency, 1913-14.—The history of the Indian currency system from 1893, when the Indian Mints were closed to the free coinage of silver, to 1914, is briefly described in paragraphs 12-43 of the Report of the Royal Commission on Indian Finance and Currency, which sat in 1913-14 under the chairmanship of the Rt. Hon. Austen Chamberlain, M.P., now Chancellor of the Exchequer. In this report, issued a few months before the outbreak of war, the Commission generally endorsed the policy and measures which had been adopted with a view to the establishment of the exchange value of the rupee on a stable basis. They made important recommendations regarding the use of gold as currency, the minting of gold in India, the development of the note-issue, the utilisation of Government balances in India and England, the sale of drafts on India and London, the constitution and location of the Gold Standard and Paper Currency Reserves, the organisation for the discharge of financial business at the India Office, and the ques-

tion of establishing a State or Central Bank in India. These recommendations were under the consideration of the Government of India when the financial and economic upheaval consequent on the outbreak of war supervened, and it was decided to postpone further action until the return of normal conditions. We shall refer in later passages of our Report to those suggestions made by the Royal Commission which more particularly concern our enquiry.

Position at the Outbreak of War.

6. Currency in circulation.—At the outbreak of war the main facts of the Indian currency system were as follows[1]:—

The Indian currency consisted of British gold coins, silver rupees, subsidiary coins of silver, nickel, and bronze, and currency notes.

The British sovereign and half-sovereign were unlimited legal tender for 15 and $7\frac{1}{2}$ rupees respectively, and the Government had undertaken by notification to issue rupees to the public in exchange for sovereigns and half-sovereigns at the rate mentioned above, being the equivalent of 1*s*. 4*d*. per rupee. The rupee (as also the half-rupee) was unlimited legal tender and was the main metallic medium for the transaction of business. Currency notes of denominations of Rs. 5 and upwards were in circulation, and were legal tender without limit of amount. They were redeemable in coin on presentation at the Currency Offices.

Sovereigns had not been minted in India before the war, but the Government of India ordinarily issued them in exchange for rupees or notes in response to any demand from the public, although they had not undertaken to do so. The extent to which gold coin actually circulated in India before the war is uncertain, but in Bombay and parts of the Punjab its use as currency was not

[1] The following information may assist readers of the Report who are not familiar with Indian terms and statistics. One lakh=1,00,000. One crore=100 lakhs=1,00,00,000. At the exchange rate of 1*s*. 4*d*. per rupee, one lakh of rupees=6,666*l*. One crore of rupees=666,666*l*. The weight and fineness of the rupee and silver dollar and of the sovereign and gold dollar are shown in the table below:—

—	Weight.	Amount of Fine Silver.
	Grains.	Grains.
Rupee	180 (one tola)	165
Silver dollar	412·5	371·25
		Amount of Fine Gold. grains.
Sovereign	123·27447	113·0016
Gold dollar	25·8	23·22

uncommon. In any case, the amount of gold coin absorbed was large, as will be seen from the figures for the five years before the war:—

Absorption of sovereigns and half-sovereigns in India.

	£
1909—10	2,873,000
1910—11	1,433,000
1911—12	8,887,000
1912—13	11,100,000
1913—14	12,070,000

7. Sale of Council Drafts.—There was normally a steady demand for remittance to India as the result of a favourable trade balance. This was adjusted partly by the importation of the precious metals, which was unrestricted, and partly by the sale by the Secretary of State in Council of drafts on the Government of India. The sale of these drafts, generally known as Council Drafts, was primarily intended to provide funds for meeting expenditure on behalf of the Government of India in the United Kingdom. It had the effect of releasing currency (metallic rupees or notes or, exceptionally, gold) in India against payment of sterling in London, and it was found convenient to extend the sales so as to provide additional currency in response to the requirements of trade. The same result would have been produced by the shipment of gold to India and its tender to the Government in exchange for rupees; but the acceptance in London of sterling (which was then equivalent to gold) instead of gold in India was convenient both for the Government and for the purchasers of Council Drafts.

The amount of the Council Drafts offered for sale each week was therefore fixed not only with reference to the requirements of the India Office, but also with reference to the demands for remittance to India, subject always to the capacity of the Government of India's resources to meet them. The rate obtained for the drafts varied from time to time according to trade demand, but as there was a standing offer to sell bills without limit of amount at 1*s*. $4\frac{1}{8}d$. per rupee, the price never exceeded this figure, which corresponded to the theoretical gold export point. The Secretary of State also maintained the practice of not selling his bills below 1*s*. $3\frac{29}{32}d$. per rupee.

Reverse Councils.—If, owing to a temporary change in the normal current of trade, there was a tendency for the exchange value of the rupee to fall below this figure, and if this tendency was not sufficiently counteracted by a cessation of the sales of drafts, the situation was met by the sale in India of bills on London, generally known as "Reverse Councils," at 1*s*. $3\frac{29}{32}d$. per rupee.

Gold Standard Reserve.—The Gold Standard Reserve, which had been accumulated from the profits on the coinage of

rupees, was available for the purpose of meeting these Reverse Drafts, thus answering the purpose for which it was created, and preventing any further fall in the exchange value of the rupee.

Stabilisation of exchange.—The effect of these arrangements was to keep the exchange value of the rupee very near to the ratio of 15 rupees to the £. Such fluctuations as occurred were similar to those that occur from time to time in the exchange between gold standard countries where the variations are limited by the cost of moving gold to adjust the balance of indebtedness.

The effective maintenance of this fixed relation depended not upon the import and export of gold, but upon the action of the Secretary of State and the Government of India in giving rupees in exchange for gold or sterling, and sterling for rupee currency, in the manner explained above. The Indian standard of value has therefore been described not as a gold standard but as a gold exchange standard. This designation, however, is open to criticism on the ground that it does not take account of the distinction which it has now become necessary to observe between gold and sterling. This distinction, as we shall see later, introduces a new and critical problem in connection with the exchange.

8. Part played by Council Drafts and precious metals in adjustment of trade balance.—The precious metals played a part little less important than that of Council Drafts in the adjustment of India's trade balance. The following table sets forth the balance of trade on private account, the net imports of treasure on private account and the sales of Council Drafts for the 10 years prior to the outbreak of war:—

	Excess of Exports over Imports on Private Account.	Net Imports of Treasure on Private Account (Gold and Silver. Coin and Bullion).	Net Sales of Council Drafts (i.e., Council Drafts less Reverse Drafts).
	£	£	£
1904—5 . .	40,548,200	16,709,600	24,150,000
1905—6 . .	39,086,700	9,646,900	31,886,000
1906—7 . .	45,506,600	14,420,000	34,069,400
1907—8 . .	31,640,000	18,253,300	15,676,700
1908—9 . .	21,173,300	11,116,300	5,335,300
Total .	177,954,800	70,137,100	111,117,400
	£	£	£
1909—10 . .	47,213,000	20,688,000	27,710,600
1910—11 . .	53,685,300	21,700,000	26,389,800
1911—12 . .	59,512,900	28,706,000	26,917,500
1912—13 . .	57,020,900	29,435,000	25,983,500
1913—14 . .	43,753,900	19,713,000	31,200,800
Total .	261,186,000	120,242,000	138,202,200

It is impossible. however, to arrive at any exact analysis of all the elements contributing to the settlement of India's trade balance, since the "invisible" exports and imports (freights, insurances, interest, transfer of profits, movements of capital, etc.) cannot be valued accurately.

EFFECT OF OUTBREAK OF WAR ON FINANCIAL POSITION IN INDIA.

9. The outbreak of war immediately caused, in India as elsewhere, a general dislocation of trade and business of which the principal symptoms were the weakening of exchange, withdrawals of Savings Bank deposits, a demand for the encashment of notes, and a run on Indian gold stocks.

Weakening of exchange.—The weakening of exchange was met by the proved expedient of offering drafts on London. Between 6th August 1914 and 28th January 1915 Reverse Councils were sold to the extent of 8,707,000*l*. In February 1915 the demand for Council Drafts revived, and, apart from further periods of weakness in 1915-16, and between November 1918 and April 1919, when Reverse Councils were sold to the extent of 4,893,000*l*. and 5,465,000*l*. respectively, Indian exchange remained strong throughout the duration of the war.

Withdrawal of Savings Bank deposits.—The net withdrawal of Savings Bank deposits amounted in the first two months of the war to Rs. 6 crores, out of the total deposits of 24½ crores on 31st July 1914. From September to October 1914 there were further withdrawals to the extent of Rs. 2 crores. Subsequently there was a recovery, but the net withdrawals for the year 1914-15 amounted to over Rs. 8 crores. The tide turned in 1915-16, and since that date deposits have continued to increase, with the result that the figure at the end of 1918-19 was 18¾ crores, There was also a run on the banks, but this proved of short duration.

10. Encashment of notes.—Some lack of confidence in the Indian note issue manifested itself at the outbreak of war and resulted in a net return of currency notes to the extent of 10 crores between 31st July 1914 and 31st March 1915, at which date the net circulation[1] had declined from Rs. 66·28 crores to Rs. 55·65 crores. The silver held in the Paper Currency Reserve fell from Rs. 33·94 crores on 31st July to Rs. 29·87 crores on 31st December 1914. But from the spring of 1915 onwards there has been a steady increase of the note circulation and on 30th November 1919 the net circulation amounted to Rs. 178·93 crores.

Demand for gold.—At the end of July 1914 there arose a keen demand for gold in exchange for notes, and between the 1st and 4th of August the Government of India lost about 1,800,000*l*. of gold. Some precautions had been taken to discourage the withdrawal of gold for internal purposes when there

[1] The term "net circulation" means the amount of notes issued ("gross circulation") less those held in Reserve Treasuries.

was a demand for its use as a means of foreign remittance; but when it was seen that the precautions were unavailing it became necessary on 5th August to suspend the issue of gold to private persons. After that time notes presented for encashment were paid in silver coin only.

The disquieting symptoms to which we have referred lasted only for a short time. The return of public confidence was assisted by the assurance given to the banking and commercial community of adequate and continuous facilities for remittance and by the readiness with which the Government of India met demands for the encashment of currency notes.

CURRENCY DIFFICULTIES.

11. Symptoms of currency difficulties.—It is not surprising that the outbreak of war should have caused a temporary disturbance of Indian financial conditions, but when the first shock had passed away the currency mechanism worked smoothly. It was not until the end of 1916 that acute complications arose in the sphere of Indian currency and exchange. These complications showed themselves mainly in the rapid rise in the price of silver and later in the increasing difficulty of obtaining silver to meet the heavy demands for silver coin. The causes contributing to these results were various, and it will be necessary to trace them in some detail.

12. Large trade balance in favour of India.—The Government of India, as is well known, are under the obligation of meeting heavy sterling payments in the United Kingdom. The net amount of these in the years 1910-14 averaged over 25,000,000*l.* a year. The ability of the Government of India to remit to London the funds required for these payments, and also the successful working of the Indian currency system, depend on the existence of a substantial balance of trade in India's favour. In the period immediately preceding the outbreak of war India had enjoyed a series of remarkably prosperous seasons, as will be seen from the following table, which exhibits the value of her exports and imports on private account for the years 1909-10 to 1913-14:—

Exports and Imports of Merchandise on Private Account.[1]

Year.	Exports. £	Imports. £	Net Exports. £
1909—10	125,253,000	78,040,000	47,213,000
1910—11	139,921,300	86,236,000	53,685,300
1911—12	151,896,100	92,383,200	59,512,900
1912—13	164,364,800	107,343,900	57,020,900
1913—14	165,919,200	122,165,300	43,753,900
Average for 5 years	149,470,900	97,233,700	52,237,200

[1] These figures represent rupee values converted at the statutory rate of Rs. 15=£1.

The corresponding figures for the years 1914-15 to 1918-19 are as follows:—

Year.		Exports.	Imports.	Net Exports.
		£	£	£
1914—15	.	121,061,100	91,952,600	29,108,500
1915—16	.	131,586,800	87,560,200	44,026,600
1916—17	.	160,591,200	99,748,000	60,843,200
1717—18	.	161,700,000	100,280,000	61,420,000
1918—19	.	169,230,000	112,690,000	56,540,000
Average for 5 years		148,833,800	98,446,100	50,387,700

It will be observed that the average balance in India's favour was slightly higher in the earlier quinquennium than in the later, mainly owing to the heavy fall in the first two years of the war. But if we take the three years 1916-17, 1917-18, 1918-19, when Indian currency difficulties were most acute, the average balance of trade in India's favour, *viz.*, 59,601,100*l.*, will be seen to have been decidedly in excess of the average of the last three years of the pre-war period (1911-12 to 1913-14), *viz.*, 53,429,200*l.*[1] During the war imports into India were limited by the restriction of the available supplies from manufacturing countries in Europe. Imports from Germany and Austria ceased entirely on the outbreak of war, whilst the productive power of the United Kingdom and her Allies was more and more completely absorbed on war industries as hostilities were protracted. There was consequently a large reduction in the quantity of goods imported into India, and it was only the rise in prices that maintained the value of the import trade and prevented its actual contraction. Exports from India, on the other hand, though restricted by difficulties of transport and finance, were in great demand. Supplies of raw materials and foodstuffs were required for the use of the Allied Powers, and the prices they realised were abnormally high. Enhanced values counteracted the shortage of freight and restrictions of finance, with the result already indicated, that the favourable trade balance was not only maintained, but even showed a tendency to increase.

13. Exceptional disbursements on behalf of His Majesty's Government, etc.—The large balance of trade indebtedness in India's favour was reflected in the strength of exchange and the heavy demand on Government for currency; and other special causes were at work during the war to intensify this demand. India formed the base of important military operations in Mesopotamia, Persia and East Africa. The Government of India were called upon to provide funds for the payment of British and Indian troops engaged, for the purchase of a large part of the supplies, and for other expenses incidental to a modern campaign, and also for meeting civil expenditure in occupied

[1] The excess would be somewhat greater if in the last two years the rupee values were converted at the then current rate of exchange.

territory. The amount of the recoverable expenditure incurred by the Government of India on behalf of the Imperial Government between 1914 and the present date has exceeded 240,000,000*l.*, and expenditure of this nature has not yet ceased. In addition to the above, arrangements were made for the financing of purchases in India on behalf of certain Dominions and Colonies and for the provision of rupee credits, amounting to 20 crores in 1917-18 and 1918-19, for American importers of Indian produce.

These exceptional disbursements created a heavy additional demand for Indian currency.

14. Decrease in imports of precious metals.—We have already referred to the part that the imports of gold and silver into India play in normal conditions in adjusting India's favourable trade balance. We shall deal later with the nature of the Indian demand, monetary, industrial, and social, for the precious metals. At present we are concerned with the deficiency in the satisfaction of this demand in the period of the war. The following table exhibits the value of India's imports of gold and silver for the five years 1909-10 to 1913-14, and the corresponding value in the years 1914-15 to 1918-19:—

Net imports into India of Treasure on Private Account.

	Gold Coin and Bullion.	Silver Coin and Bullion.	Total.
	£	£	£
1909—10 . .	14,446,000	6,242,000	20,688,000
1910—11 . .	15,986,000	5,714,000	21,700,000
1911—12 . .	25,178,000	3,528,000	28,706,000
1912—13 . .	25,052,000	4,383,000	29,435,000
1913—14 . .	15,550,000	4,163,000	19,713,000
Total .	96,212,000	24,030,000	120,242,000
	£	£	£
1914—15 . .	5,637,000	6,676,000	12,313,000
1915—16 . .	3,267,000	3,717,000	6,984,000
1916—17 . .	2,797,000	*—1,440,000*	1,357,000
1917—18 . .	14,306,000	971,000	15,277,000
1918—19 . .	15,000	38,000	53,000
Total .	26,022,000	9,962,000	35,984,000

Several factors contributed to the remarkable decline in the import of the precious metals during the latter period.

The first, and far the most important, factor was the difficulty of obtaining gold. The free market in London, on which India had been able to draw in the past, disappeared on the outbreak of war. Restrictions on the export of gold were imposed by belligerent Governments desirous of maintaining their stocks of the metal for war purposes, and India was accordingly only able to obtain very limited quantities. The relatively high

imports in 1917-18, mainly from Japan and the United States, were largely caused by the difficulty of obtaining rupee exchange when the sales of Council Drafts were limited and controlled. The low figure for 1918-19 was mainly due to restrictions placed upon the export of gold from the United States.

15. Shortage of silver supply.—The dearth of gold created a strong demand for silver. This would have tended normally to increase private imports of silver, which remained unrestricted until September 1917. But during this period of the war the silver market was subject to conditions of supply and of demand which severely limited the amount of the metal available for private purchasers.

There was, in the first place, a great shortage of supply. The world's production of silver from 1914 onwards exhibited a marked decline from the production of the preceding years. The question is fully discussed in the Report on the World's Production of Silver, by Professors Carpenter and Cullis, which is included in the Appendices to our Report. Their statistics are summarised in the following table:—

Mine Production of Silver (in Fine Ounces, 000 omitted).

Year.	Canada.	United States of America.	Mexico.	Rest of World.	Total of World.
1910	32,869	57,599	71,372	57.249	219,089
1911	32,559	61,109	79,033	57.683	230,384
1912	31,956	66,041	74,640	60,423	233,060
1913	31,805	71.200	70,704	57,966	231,676
Average for 4 years 1910—1913 .	32,297	63,987	73,937	58.331	228.552
1914	28,449	69,634	27,547	50.418	176,048
1915	26,626	72,369	39,570	47,180	185,745
1916	25 460	78,875	22,838	48,283	175,456
1917	22,221	70,666	31,214	50,919	175,050
Average for 4 years 1914—1917	25.689	72.886	30,292	49,208	178,075

Approximately three-quarters of the world's silver is mined in North America and Mexico. The decrease in the Canadian production due to the progressive exhaustion of the Cobalt field was more than compensated by an increase in the production of the United States of America, and the key to the shortage of silver is to be found in Mexico, where, owing to political disturbances, the production of silver fell from an average of

73,937,000 fine ounces for the years 1910-13 to an average of 30,292,000 fine ounces for the years 1914-17, a reduction of 43·6 million ounces out of a total reduction of 50·5 milion ounces in the world's production. It will be noted that the fall in Mexican production, though it coincided approximately with the beginning of the war, was not caused by the war, but by internal conditions in Mexico.

16. Heavy world demand for silver.—Had the world's demand for silver remained normal, the marked decline in supplies from 1914 onwards could hardly have failed to produce a rise in price and must have influenced the quantity of the metal available for India. But actually the world's demand for silver was unusually keen, particularly for coinage. The coinage of the British Empire for example absorbed nearly 108 million fine ounces of silver in the years 1915 to 1918 as against 30·5 million fine ounces in the years 1910 to 1913, and there is evidence that there were similar increases in the silver coinage of other countries.

There has also been a heavy demand for China during the last two years. In the years 1914-17 China was a seller of silver and her net exports of the metal amounted to over 77,000,000 standard ounces. From 1918, on the other hand, China has been a persistent buyer, and in recent months the intensity of her demand has been the dominating feature of the silver market. It is probable that the export of the previous years has now been made good, but so far there is no indication of any slackening in the demand.

17. Indian demand for silver for coinage.—We have seen that war conditions militated against the normal flow of the precious metals to India, where their import would have assisted in the liquidation of the trade balance in India's favour. The burden of liquidating this balance was thus focussed on the Government of India and took the form of heavy demands for currency. The efforts made to meet these demands are indicated by the fact that between April 1916 and March 1919 over 300,000,000 standard ounces of silver[1] were bought in the market for coinage in addition to 200,000,000 fine ounces purchased under the Pittman Act (*see* paragraph 23), as compared with about 180,000,000 standard ounces between April 1904 and March 1907, when the Indian demand was specially heavy and continuous.

18. Rise in price of silver.—These large purchases, combined with the decrease in the supplies of silver and the increased demand from other quarters, reacted strongly on the price of the metal. In 1915 the highest price of silver in the London market was 27¼*d.* per standard ounce. By April 1916 it had risen to 35⅛*d.* and in December had reached 37*d.* The rise in price continued throughout the first part of 1917 and in August it exceeded 43*d.* We invite attention to this figure, because it marks the point at which the exchange value of the

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[1] Standard silver is 925 fine.

rupee at 1*s.* 4*d.* is equivalent to its bullion value, and it was the rise in the price of silver to this figure and above it that necessitated the alterations in exchange to which we refer in paragraph 22. In September 1917 the price of silver rose to 55*d.*

In September 1917 the United States Government instituted control over the trade in silver and prohibited the export of the metal except under licence. The effect of this control was to check the rising tendency of silver prices, and between October 1917 and April 1918 the London quotation varied between 41$\frac{7}{8}$*d.* and 49$\frac{1}{4}$*d.* per standard ounce. After the passing of the Pittman Act in April 1918 (*see* paragraph 23), no export licenses were granted by the Government of the United States of America except for silver which was bought at 101$\frac{1}{2}$ cents, or less, per fine ounce, and was required for purposes connected with the prosecution of the war. Similar measures were adopted by the Canadian Government, and the British Government fixed a maximum price for silver corresponding to the American maximum. These measures had the effect of stabilising the market price of silver at about a dollar per fine ounce, and facilitated purchases for India. Between May 1918 and April 1919 the London price for silver ranged between 47$\frac{3}{4}$*d.* and 50*d.* per standard ounce. But when in May 1919 the United States Government and the British Government withdrew control over the silver market, a further rise in price occurred, and in May the London price reached 58*d.*, or more than double the maximum attained in 1915. Since that date, mainly on account of the exceptional demands from China, the price has risen still further and on 17th December stood at 78*d.* per standard ounce.

19. Influence of dollar-sterling exchange on London price of silver.—It is necessary at this stage to refer to another factor tending to raise the price of silver in the London market. During the war arrangements were concerted between the British and American Governments under which the sterling exchange on America was "pegged" at \$4·76$\frac{7}{16}$. Government support of exchange was withdrawn on 20th March 1919 and since that date the London-New York exchange has moved heavily against the United Kingdom. On 17th December the £ sterling was equivalent to only \$3·83 as against its par value of \$4·8666. As America is the principal source of the world's silver supply, the chief payments for the metal have to be made ultimately in that country. The sterling price of silver accordingly takes account of the state of the London-New York exchange, and any rise or fall in that exchange is reflected in the London price. A fall in sterling exchange has thus the effect of raising the London quotation for silver. For any given sterling value of the rupee there is a corresponding sterling price for silver above which silver for coinage into rupees can only be purchased at a loss. If, without any change in the gold price of silver as measured in dollars, the London quotation should rise in consequence of a

fall in the London-New York exchange, purchases of silver for India may be rendered impracticable unless the rupee exchange is raised to redress the fall in sterling. The position may be made clear by an illustration. If the exchange value of the rupee is 2*s.*, the Secretary of State can buy silver for coinage into rupees without loss at 63*d.* per standard ounce. If the London-New York exchange fell 10 per cent., the sterling quotation for silver would, *ceteris paribus*, react in proportion, and assuming that the price stood at 63*d.* before the fall in American exchange, it would rise to over 69*d.* as the direct consequence of the fall in exchange. If in these conditions the Secretary of State wished to purchase silver for coinage without loss, it would be necessary for the rupee exchange to be raised to about 2*s.* 2½*d.*

20. Maintenance of pre-war currency system impracticable.—In the circumstances we have described the purchase of silver for coinage was attended with serious difficulty. In paragraph 23 we give details of the purchases made. Though these purchases represent a considerable proportion of the world's annual supply, they were insufficient for the heavy and continuous requirements for silver coin. This fact, taken in conjunction with the rising price at which purchases had to be effected rendered the maintenance of the pre-war currency and exchange system impracticable. The Secretary of State was unable to maintain his offer to sell Council Drafts without limit of amount, while in view of the rise in the price of silver to a level higher than that which corresponds to a bullion value of 1*s.* 4*d.* for the rupee, he was compelled to raise the rate at which he sold the limited amount of Council Drafts which he was able to offer.

These fundamental changes in the system were accompanied by a number of supplementary measures designed to meet special difficulties which arose from time to time. We propose to deal first with the changes in the machinery for regulating exchange, *viz.*, (*a*) the Government control of exchange and (*b*) the raising of the rate for the sale of Council Drafts, and then to pass on to the other measures adopted by the Government to conserve their resources and to meet the exceptional demands for currency.

Measures taken.

(*a*) *Control of Exchange.*

21. After exchange had recovered from the temporary dislocation consequent upon the outbreak of war, the demand for Council Drafts continued on a normal scale until October 1916. During November the amount of the weekly sales increased rapidly, and in the first fortnight of December they exceeded 5,000,000*l.* The rupee holding in the Paper Currency Reserve had then fallen to 14 crores, and though there was silver awaiting coinage and the Secretary of State had made large purchases, it was evident

that the continuance of sales on this scale would endanger the convertibility of the note issue.

Limitation of sales of Council Drafts.—To avoid this danger the Council Drafts sold by the Secretary of State were limited from 20th December 1916, the weekly amount, which varied between 120 lakhs and 30 lakhs, being fixed from time to time mainly on a consideration of the rupee resources of the Government of India. The limitation of the amount of Council Drafts at a time when the demand for remittance to India was exceptionally strong and no adequate alternative method of remittance was available led to a divergence between the market rate of exchange and the rate at which the drafts were sold. It also became evident that the remittance available might be insufficient to finance the whole of the Indian export trade, and it was essential that the exports required for war purposes should not be impeded. It was found necessary, therefore, to introduce certain measures of control.

Sale at fixed rate to selected institutions on specified conditions.—From 3rd January 1917 Council Drafts were sold at a fixed rate, which at the outset was 1*s.* $4\frac{1}{4}$*d.* for immediate telegraphic transfers, and the sale was confined to banks and firms on the "Approved List," which included the chief exchange banks and a few large purchasers of drafts. A little later these banks and firms were required to do business with third parties at prescribed rates and to apply their resources primarily to financing the export of articles of importance to the Allies for the purpose of carrying on the war, a list of which was drawn up by the Secretary of State. An appeal was at the same time addressed to other firms engaged in Indian trade to conduct their remittance transactions through the exchange banks.

Over-buying guarantee to exchange banks.—Further, in order to encourage the exchange banks to buy export bills in excess of their purchases of exchange in the other direction, the Secretary of State insured them against the risk of a rise in exchange, by undertaking to sell to them within a year after the war exchange up to the amount of their overbuying at the rate at which their excess purchases had been made.

This scheme of Government control constituted a complete departure from the system of free and unlimited remittance that prevailed before the war, and was naturally unpalatable to the commercial community. But the evidence we have taken shows that the intervention of Government was regarded as inevitable in the circumstances and it was due largely to the hearty co-operation of the exchange banks and trading firms with the Government that the market rate of exchange was maintained near the rate at which Council Drafts were sold and the necessary finance was successfully provided for the large volume of exports of national importance.

Termination of control.—After the conclusion of the armistice the necessity for reserving finance for particular exports ceased. The overbuying guarantee was in due course terminated, and the list of articles to which priority of export finance was given was abolished. On the withdrawal of these restrictions, importers were naturally unwilling to continue incurring loss by effecting homeward remittances through the exchange banks, and a considerable business was transacted between importers and exporters direct at rates appreciably higher than the rate for Council Drafts. Meanwhile, the revival at the end of July 1919 of a free market for gold, to which we shall refer below, provided an alternative method of remittance, and facilitated the return to more natural conditions than had been possible during the latter part of the war. From 18th September 1919 drafts have been sold by open competitive tender, subject to a minimum rate and subject to the condition that no applicant may apply for more than 20 per cent. of the amount offered each week. The amount of drafts offered weekly is fixed on a consideration of the trade demand and the resources of the Government of India.

(b) Raising of Rate for Sale of Council Drafts.

22. Rise in exchange.—The rise in the price of silver to a point at which the bullion value of the rupee exceeded 1*s.* 4*d.* made the sale of Council Drafts at the rates fixed on 3rd January 1917 impossible, except at a loss to Government. There was also a danger that if the rupee were undervalued it would tend to disappear from circulation, to be melted down and possibly to be exported. These tendencies probably existed in any case owing to the prohibition of the import of silver, but would have been aggravated by any undervaluing of the rupee. These considerations led to a series of changes in the rate of exchange. The first of these changes took place on 28th August 1917, when the rate for immediate telegraphic transfers was raised from 1*s.* $4\frac{1}{4}$*d.* to 1*s.* 5*d.* Shortly afterwards the Government of India announced that the price at which Council Drafts would be sold in future would be based roughly on the price at which silver could be bought, and this policy has governed alterations in the rate of exchange up to the present time. On 12th April 1918, in consequence of the agreement with the United States Government for the purchase of silver from the dollar reserve at $101\frac{1}{2}$ cents per fine ounce, the price for immediate telegraphic transfers was raised to 1*s.* 6*d.* This rate was maintained until 13th May 1919, when the removal of the American control over the export of silver led to a rise in the price of the metal and necessitated a further rise to 1*s.* 8*d.* While we have been conducting our enquiries, the price of silver has broken all records, and the rate has been raised successively to 1*s.* 10*d.* on 12th August 1919, to 2*s.* on 15th September 1919, to 2*s.* 2*d.* on 22nd November 1919 and to 2*s.* 4*d.* on 12th December 1919. The last figure is now the

minimum rate for the sale of immediate telegraphic transfers by competitive tender, while the Secretary of State has announced that he will sell reverse immediate telegraphic transfers at the rate of *2s.* $3\frac{29}{32}$*d.* if the demand for them should arise. Thus the rate of exchange has been raised by successive steps from *1s. 4d.* to *2s. 4d.*, as shown in the following table:—

Date of introduction.	Minimum Rate for Immediate Telgraphic Transfers.	
3rd January 1917	1	4¼
28th August 1917	1	5
12th April 1918	1	6
13th May 1919	1	8
12th August 1919	1	10
15th September 1919	2	0
22nd November 1919	2	2
12th December 1919	2	4

(*c*) *Purchase of Silver.*

23. These modifications of system would not have been effectual in meeting the situation unless special measures had also been taken to increase the supply of currency. In February 1916 the necessity for rupee coinage on a large scale became apparent and the Secretary of State began to purchase silver.

Large purchases in the market.—In 1915-16 and the subsequent years he bought in the market the amounts shown below.

Prohibition of import.—To facilitate his operations, by excluding from the market Indian buyers who would otherwise have bought for non-coinage purposes, the import of silver into India on private account was prohibited on the 3rd September 1917. This measure, however, removed only a few of the smaller competitors for the world's diminished supply of silver, and the world demand remained so heavy that it was impossible to satisfy India's demand without tapping sources of supply outside the ordinary market.

Acquisition of dollar silver from U. S. A.—The Government of the United States of America, therefore, were approached, through His Majesty's Government, on the subject of releasing a portion of the silver dollars held in their reserve. These representations met with a ready response, and on 23rd April 1918 the United States Congress passed the Pittman Act, which authorised the sale to other Governments of silver not exceeding 350,000,000 silver dollars from the holding in the dollar reserve. Of this amount the Government of India acquired 200,000,000 fine ounces at 101½ cents per fine ounce. Delivery in India began in July 1918, and was spread over a period of about a year. The timely help thus rendered by the United States Government in placing at India's disposal a supply of silver which

represents considerably more than the world's annual mine production since 1914, enabled the Government of India to tide over a very serious currency crisis and to maintain the convertibility of the note-issue.

The following table shows the amount of silver purchased by the Secretary of State in the last five years:—

	In open Market (Standard Ounces.	From United States Dollar Reserve (equivalent in Standard Ounces).
1915—16	8,636,000	—
1916—17	124,535,000	—
1917—18	70,923,000	—
1918—19	106,410,000	152,518,000
1919—20 (to 30th November 1919)	14,108,000	60,875,000
Total .	324,612,000	213,393,000

The total amount is thus 538,005,000 standard ounces.

(d) Measures for Conservation and Economy of Silver.

24. Prohibition of export and melting.—These special measures for obtaining silver were supplemented by endeavours to protect the currency against depletion by export or melting. From 29th June 1917 the use of silver or gold coin for other than currency purposes has been illegal, and from 3rd September 1917 the export of silver coin and bullion from India has been prohibited except under license.

Issue of notes of small denominations and new nickel coins.—Steps were also taken to economise silver by the issue of Rs. 2½ and one-rupee notes, to which we shall refer in more detail below, and by extending the use of nickel for coin of small denominations. At the end of March 1918 a new two-anna nickel coin was issued to replace the silver two-anna piece, and this new coin has been so readily accepted that legislation was passed in September 1919 authorising the issue of four-anna and eight-anna nickel coins. The eight-anna nickel piece will not be unlimited legal tender like the corresponding silver coin; it will be legal tender up to one rupee only. We understand that the new coins will be issued at an early date.

(e) Acquisition and Use of Gold.

25. Acquisition of imported gold.—In view of the shortage of silver it was important that the Government stock of gold should be as large as possible. With this object an Ordinance was issued on 29th June 1917, requiring all gold imported into India to be sold to Government at a price which, being based on the sterling exchange value of the rupee, took no account of

the premium on gold as compared with sterling. The gold so obtained was placed in the Paper Currency Reserve as a backing against the issue of additional notes.

Coinage of gold.—To enable the gold bullion and foreign coin held by the Government of India to be converted into sovereigns without the delay involved by sending it to Australia for coinage and return, a branch of the Royal Mint was opened in Bombay in August 1918. Pending the establishment of the Royal Mint, the gold mohur, a 15-rupee coin of the same weight and fineness as the sovereign, was minted as an emergency coin in order to supplement the stock of sovereigns available for issue as currency during the crisis of 1918. 2,110,000 gold mohurs and 1,295,000 sovereigns were coined in Bombay before the suspension of gold coinage in April 1919, when in view of difficulties in supplying the necessary staff it was decided to close temporarily the branch of the Royal Mint.

Gold as currency.—As we have mentioned above, the issue of sovereigns was stopped shortly after the outbreak of war. Owing to the demand for gold for social and industrial purposes and the restricted supply, the bazaar price of the sovereign gradually rose and remained considerably above its statutory rate of Rs. 15. This premium on gold precluded its use as currency except in emergencies, but on two occasions attempts were made to prevent a further diminution of the rupee stocks by the issue of gold. At the beginning of 1917 gold bullion of the value of about 4,000,000*l*. was sold and subsequently sovereigns to the amount of about 5,000,000*l*. were issued for the purchase of crops in certain areas. Again, from February 1918 sovereigns and gold mohurs amounting to nearly 6,000,000*l*. were issued for the financing of certain crops. The earlier issue of sovereigns was coincident with a large return of rupees from circulation, especially in those districts where sovereigns had been issued, but in 1918 the issue of gold was not followed by a return of rupees.

26. Recent measures for acquisition of gold.—During the war the amount of gold which could be obtained by India was limited by the restrictions on its export from belligerent countries. The removal of the embargo on the export of gold by the United States Government on the 9th June 1919, and the freeing of the market for South African and Australian gold enabled India to obtain a larger supply. From 18th July 1919, immediate telegraphic transfers on India were offered against deposit at the Ottawa Mint of gold coin or bullion at a rate corresponding to the prevailing exchange rate. Very little gold was obtained from this source, and the arrangement was terminated on 15th September 1919. From 22nd August 1919 a limited amount of immediate telegraphic transfers on India were offered weekly for sale by competitive tender in New York, the proceeds of the sales being remitted to India in gold. Towards the end of October the demand for these transfers fell off and the sales

were discontinued. The amount of gold obtained in this way was about 467,000[1] fine ounces. Arrangements were also made for the direct purchase of gold in London, the United States and Australia, and by 30th November 1919 about 2,485,000 fine ounces had been purchased. Finally, on 15th September 1919, the rate paid by the Government of India for the acquisition of gold brought into India on private account was fixed so as to include the premium on gold over sterling as measured by the dollar-sterling exchange, and has been varied from time to time approximately in accordance with the fluctuations of this exchange. The effect of the change in the basis of the acquisition rate was to re-establish an effective gold point, and to facilitate the import of gold in payment for exports as an alternative to the purchase of Council Drafts. The amount of gold imported on private account and tendered to the Government of India between 15th September and 30th November was approximately 345,000 fine ounces.

27. Sales of gold.—In order to make a portion of the gold so obtained available for the use of the public of India, the Government of India announced, at the end of August 1919, that sales of gold would be held fortnightly until further notice, and that in each of the first three months not less than the equivalent of the gold content of 1,000,000 sovereigns would be offered for sale. The amount offered at the second sale in November was increased to 500,000 tolas (equivalent to nearly 800,000 sovereigns), and it was announced that this amount would be offered fortnightly for the three months beginning from December. The immediate effect of these sales was a considerable drop in the bazaar price of gold. The price of English bar gold fell from Rs. 32·12 per tola (Rs. 20·9 per sovereign) on 15th August to Rs. 27 per tola (Rs. 16·5 per sovereign) on 22nd September, but by the end of October the market had recovered and the price was Rs. 29·12 per tola (Rs. 18·11 per sovereign). At the beginning of December the price had again fallen to Rs. 28·5 per tola (Rs. 17·11 per sovereign). The total amount of gold sold up to 30th November amounted to about 2,159,000 tolas, being the equivalent of the gold content of about 3,439,000 sovereigns.

(*f*) *Increase in the Note Issue.*

28. Expansion of note circulation.—The difficulties of obtaining sufficient quantities of the precious metals for coinage purposes, and as backing for the issue of additional notes, made it necessary to increase the fiduciary portion of the note issue. Prior to the war the invested portion of the Paper Currency Reserve was limited by law to 14 crores of rupees. Since the beginning of November 1915 the legal limit of the invested portion of the Reserve has been modified nine times and now stands at

[1] 100 ounces of fine gold is the equivalent of the gold content of 425 sovereigns.

120 crores, of which 20 crores may be invested in securities of the Government of India. During this period the gross circulation of notes has increased nearly threefold, while the percentage of metallic backing has decreased by nearly one-half. The following table shows the growth of the circulation and the changes in the composition of the Reserve:—

Date.	Lakhs of Rupees.					Percentage of Total Metallic Reserve to gross Note Circulation.
	Gross Note Circulation.	Composition of Reserve.				
		Silver.	Gold.	Securities.	Total.	
31st March 1914	66,12	20,53	31,59	14,00	66,12	78·9
Do. 1915	61,63	32,34	15,29	14,00	61,63	77·3
Do. 1916	67,73	23,57	24,16	20,00	67,73	70·5
Do. 1917	86,38	19,22	18,67	48,49	86,38	43·9
Do. 1918	99,79	10,79	27,52	61,48	99,79	38·4
Do. 1919	153,46	37,39	17,49	98,58	153,46	35·8
30th November 1919	179,67	47,44	32,70	99,53	179,67	44·6

The use of paper currency was further stimulated by the issue in December 1917 and January 1918 of notes for Rs. 2½ and one rupee respectively, to supplement the notes of Rs. 5 and higher denominations already in circulation. At first these notes of small denomination did not circulate to any appreciable extent, but later, when the supply of rupees was curtailed, their circulation increased rapidly, and on 31st March 1919 the gross circulation exceeded Rs. 1,84 lakhs in the case of the Rs. 2½ denomination and Rs. 10,50 lakhs in the case of the one-rupee denomination.

29. Restrictions on facilities for encashment.—The encouragement of the use of notes by the provision of ample facilities for their encashment had been one of the most prominent features of the currency policy of the Government of India in the years preceding the outbreak of war, and this policy was continued as long as the supply of rupees was adequate. From 1916, owing to the causes which we have already indicated, the absorption of rupees was abnormally large, the figure for 1916-17 being Rs. 38,81 lakhs and for 1917-18 Rs. 27,86 lakhs; and on 1st April 1918 the silver balances had fallen to under 10½ crores, or about 8 crores less than what was considered a safe minimum in the period before the war. The unfavourable war news in March and April 1918 caused a run on the Bombay Currency Office for the encashment of notes, and this was followed by similar difficulties elsewhere, notably in Lahore. Inconvertibility appeared to be inevitable, and was only averted by the energy and resource of the officers responsible, and by the timely announcement of the

acquisition of the Pittman silver. By the first week in June the rupee balance had diminished to little more than 4 crores. From July the delivery of the Pittman silver commenced and the situation gradually improved, but the necessity for conserving their reduced stock of rupees had forced on the Government a reversal of their previous policy. Facilities for the encashment of notes at district Treasuries were in a large degree withdrawn. The conveyance of specie by rail and river steamer was prohibited, and an embargo was placed on its transmission by post.[1] Later, in January 1919, owing to the practical administrative difficulties of dealing in full with the demands for encashment at the Currency Offices during the busy season, the daily issues of rupees to single tenderers of notes were limited to a figure which made it practicable to satisfy large demands in part and small demands as a rule in full. The result of these restrictions was the substitution to a large extent of notes for rupees as the common circulating medium.

The evidence which we have had regarding the extent of this substitution, and the ease with which it was accomplished, is rather indefinite. The continued abnormal absorption of rupees —Rs. 45,02 lakhs were absorbed in 1918-19—points to a very large use of rupees as currency. On the other hand, there is little doubt that large quantities of rupees have been retained as a store of value or have been used for industrial purposes in spite of the prohibition of melting, while the purchase of jute, cotton and other crops from the cultivators has recently been effected almost entirely by means of notes. There was in many parts of India a considerable discount on notes, especially the new Rs. 2½ and one-rupee notes, when they were first issued in large quantities to replace rupees. Discounts as high as 15 per cent. and 19 per cent. have been reported; but the discount rapidly diminished when it was seen that the notes were freely accepted in payment of Government dues and when small coin was made available in large quantities. The reports received by the Government of India in the year 1919 do not show any discount on the notes as compared with silver coin exceeding 3 per cent.

Financial Measures.

30. Other financial measures affecting currency position.—Our summary would be incomplete without a brief reference to other financial measures which affected the currency situation indirectly. Throughout the war ordinary expenditure and, in particular, capital expenditure were kept as low as possible, while from 1916-17 onwards additional taxation was imposed which, together with the normal growth of revenue, raised the total revenue of the Government of India from 84,413,500*l.* in 1915-16 to an estimated figure of 123,404,200*l.*[2] for 1919-20. The resources available for meeting the heavy war expenditure in

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[1] The restrictions on the movement of gold were removed in September 1919.
[2] At the conventional exchange of 1*s.* 4*d.* per rupee.

India were further increased by extensive borrowing in India. The loans of 1917, 1918 and 1919 yielded about Rs. 130 crores and from October 1917 short-term Treasury Bills have been issued in considerable quantities, the amount outstanding on 30th November 1919 being about Rs. 65·58 crores.

These measures materially assisted towards meeting the heavy demand for remittance to India.

Summary of Present Position.

31. Summary of existing position.—We may now summarise the main facts of the present position. Council Drafts are being sold by competitive tender, subject to a minimum rate, at present 2*s.* 4*d.* sterling, the amount being fixed weekly by the Secretary of State. It has been announced that reverse immediate telegraphic transfers will be sold at the rate of 2*s.* $3\frac{29}{32}$*d.* if the demand for them should arise. All gold imported into India has to be sold to Government at a prescribed price. The rate fixed contains an allowance to cover the premium on gold over sterling. As there is now a free market for gold, this import acquisition rate, which is varied from time to time in accordance with the movement of the dollar-sterling exchange, fixes an upper gold point which tends to prevent the rate bid for Council Drafts from rising above the minimum rate by much more than the cost of shipping gold, except possibly for short periods when the demand for remittance is urgent. The rate in force for the sale of Reverse Councils fixes a limit to the fall of exchange so long as the means for meeting them are available.

The sovereign is still legal tender in India for Rs. 15, and the Government is under an obligation to pay Rs. 15 for sovereigns presented for encashment. As, however, the bazaar price of gold is considerably above this parity, sovereigns have disappeared from circulation and are not being issued by Government. The import and export of silver are prohibited, and its price is at a level which prevents purchases by the Secretary of State for coinage except at a loss. The restrictions on the encashment of notes to which we have referred in paragraph 29 are still in force.

32. Appreciation of officials connected with Indian currency administration.—We have now completed our sketch of the developments in the Indian exchange and currency system since 1914. Before passing on from this section of our Report, those of us who are not connected with Indian official administration desire to place on record our recognition of the skill, courage and resource which the Government of India and the authorities at the India Office have shown in dealing with the complicated and ever-changing problems that presented themselves throughout the latter part of the war in connection with the Indian currency system.

CONCLUSIONS AND RECOMMENDATIONS.

33. Introductory.—Having traced the history of the Indian currency system during the period of the war we proceed to state the conclusions which we draw from it, and our recommendations for future action.

The system built up since 1893 worked well, and was beneficial to India. It supplied suitable media for the internal circulation, provided means for the settlement of the balance of trade, and secured stability between the rupee and sterling, which until recently was in practice synonymous with gold. It has proved effectual in preventing the fall in value of the rupee below 1*s*. 4*d*., and unless there should be profound modifications in India's position as an exporting country with a favourable trade balance, there was no reason to apprehend any breakdown in this respect.

But the system was not proof against a great rise in the value of silver. In framing it this contingency had not been taken into account. So little was it anticipated, that the system was not criticised on this ground, so far as we are aware, by any of the witnesses who have appeared before the successive Committees and Commissions on Indian currency. But the unexpected has happened. The price of silver has risen to unprecedented heights, partly, as we have seen, owing to the shortage of supplies from Mexico (caused by internal conditions independent of the war), and partly owing to causes arising out of the war, with the result that there has been extreme difficulty in obtaining the silver required for Indian currency, that the convertibility of the note issue has been in danger, and that the exchange value of the rupee has been raised by successive steps from 1*s*. 4*d*. to 2*s*. 4*d*.

STABILITY OF EXCHANGE: ITS ADVANTAGES.

34. The terms of our reference place before us as one of the objects of our enquiry the re-establishment of stability. We find it necessary, before formulating our recommendations, to examine in what respects exchange stability is important, and what degree of urgency attaches to its re-establishment.

Advantages to trade.—The evidence we have received was unanimous as to the benefit which India has derived from the maintenance of a fixed rate of 1*s*. 4*d*. per rupee for the 20 years from 1898 to 1917; but some witnesses expressed the opinion that fixity is not indispensable. Our conclusion, after considering the views put before us, is that, for the current operations of trade, stability is an important facility rather than an essential condition. There are many instances, including that of India herself before the closing of mints, which show that trade has flourished, and can flourish, with a fluctuating exchange. The conditions are somewhat more speculative, but the difficulties which may arise are not insuperable, and the banks are not slow to supply machinery which enables the merchant to cover his risks.

This is specially true of day-to-day fluctuations of exchange of moderate scope of the movements are of greater extent and produce large changes in the basis of relative values, a different set of considerations comes into play. For a time, at any rate, a large rise in exchange tends to stimulate the import trade and to impede the export trade, while the reverse effect is produced by a fall in exchange. If exchange is made stable at a new level we believe that these effects are in the main transitory, and do not continue beyond the period necessary for wages and other elements of cost to adjust themselves to the new conditions. But this process of adjustment is a difficult and sometimes a prolonged one, and causes severe strains in the social fabric.

35. Advantages in connection with movements of capital.—The question must also be considered in relation to the movements of capital. Stability is a necessary condition for the free investment of external capital in India as well as for the protection of capital already invested. The effect on new investments may be less important in the next few years, since it is to be anticipated that Indian capital will play an increasing part in the development of Indian resources, and that owing to the urgent demands arising in the United Kingdom and elsewhere, the supply of external capital available for India may be comparatively small. The above observations apply specially to permanent or long-term investment; but they are also true as regards the more liquid employment of money. A stable exchange facilitates the free movement of funds to and from India, thus assisting commercial finance and tending to avert temporary stringencies.

Special objections to instability under non-automatic system.—Whatever the evils and inconveniences of instability may be, they are increased if the movements of exchange are brought about not by the automatic action of economic causes, but by administrative acts. The commercial community are prepared to deal with fluctuations in exchange as well as with fluctuations in the other elements entering into a transaction, and to provide against any risks that may arise; but they feel that if official action intervenes to interpret the play of natural forces and to give effect to them, an element of uncertainty is introduced which is beyond their reckoning. However complete the integrity and however great the intelligence on which official action is based, an automatic system, which does not depend upon such action for its operation, is greatly to be preferred.

36. Conclusion as to importance of stability.—Our conclusion, therefore, is that a stable level of exchange gives the most healthy condition for production and trade, and for the employment of capital, and that large changes in the exchange value of a currency are an evil, which should be avoided so far as possible; but if a large change has taken place it may be preferable to establish stability at the new level rather than to submit to the further change which is necessary for a return to

the old level, especially if the former course shortens the period of uncertainty.

The object should therefore be to restore stability to the rupee at as early a date as practicable, and also to restore the automatic working that characterised the Indian currency system in the past.

Suggested Modifications of System.

37. It will be convenient to consider, first, certain special proposals that aim at giving stability to the exchange value of the rupee in such a way as to avoid the necessity for following the price of silver to higher levels, or, in the view of some witnesses, with the object of making it possible to revert to a value for the rupee not much above the old level of 1*s*. 4*d*. In a later part of this Report (paragraphs 44-54) we give our reasons for considering a high exchange value to be preferable to a low value; but as the proposals to which we refer are inadmissible on other grounds, it is desirable to deal with them at the outset.

(i) *Reduction of the Fineness or Weight of the Rupee.*

38. Issue of rupee of lower silver content impracticable.—It has been suggested that a new rupee should be issued having a lower silver content than the present coin. If the existing standard of fineness or the weight were sufficiently reduced, it would be possible to fix the exchange value of the rupee at any level that might be chosen, and to maintain its token character however great the rise in the price of silver might be.

The evidence we have taken was decisively hostile to this proposal. It has been urged in support of it that in the Straits Settlements and elsewhere the reduction of the silver content of full legal tender coins has been successfully made; but in none of the cases brought to our notice were the conditions similar to those existing in India. The fineness of the present rupee, which is known to every village goldsmith and silversmith, has remained unaltered since 1835, and its use is so firmly rooted in the habits of the Indian people as to have given it the character of a standard weight. Modification of the fineness or weight of the standard coin of the country would, we have been assured, react gravely on the credit of the Government, and possibly lead to serious social and economic consequences. A new rupee of lower silver content would, in accordance with Gresham's law, tend to drive the present rupee out of circulation, and very large quantities of the new rupees would be required to meet demands for metallic currency. Even if the problem of minting on the scale required could be overcome, there might be great difficulty in obtaining the necessary supplies of silver either from existing currency or otherwise. We concur, therefore, in the view of the Government of India that proposals of this character must be dismissed as impracticable.

(ii) *Issue of 2- or 3-Rupee Coins of lower proportional Silver Content.*

39. Objections to 2- or 3-rupee coins of low silver content.—A suggestion of a similar nature is that while the shortage of silver continues, 2- or 3-rupee pieces of lower proportional silver content than the rupee should be issued, with the intention that they should circulate side by side with the existing rupee, the coinage of which would be temporarily suspended. This proposal is open to many of the objections stated in the previous paragraph. Rupees would tend to disappear from circulation before the competition of the new and baser coins, and the credit of the Government would be affected by the decision to stop the minting of the coin to which India has been so long accustomed. Moreover, a 2- or 3-rupee unit would be inconveniently large for the great bulk of retail transactions in India.

(iii) *Nickel Coins.*

40. Nickel rupee not recommended, but subsidiary nickel coins approved.—For the same reasons we are unable to support the suggestion that a nickel rupee should be issued, either alone or in association with 2- or 3-rupee pieces of lower proportional silver content than the existing rupee; but we welcome the recent legislation of the Government of India authorising the issue of 4-anna and 8-anna nickel coins. Witnesses who have appeared before us have emphasised the fact that the reluctance to use Rs. 2½ and one-rupee notes when these were first issued in large quantities was due in great measure to the difficulty of obtaining small change. We hope that abundant supplies of the new nickel coins will be made available as soon as possible, and if the low legal tender limit of one rupee for the 8-anna nickel piece should prove an obstacle to its free circulation the question of raising the limit to Rs. 5 or Rs. 10 should be considered.

(iv) *Inconvertible Note Issue.*

41. Convertibility of note issue essential.—Another proposal aiming at the establishment and maintennance of a stable exchange, even though silver should continue to rise in price, is that which was put forward by the Government of India[1] before our enquiry began. Circumstances have changed since then, especially by the establishment of a free gold market, and the later proposals of the Government of India[2] are of a different character; but it is necessary to explain the reasons against the adoption of the earlier proposal.

It was proposed that exchange should be stabilised at a rate which could reasonably be expected to afford an assurance that the rupee would remain a token coin. If, contrary to expectations, the price of silver should rise to a height which would defeat this

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[1] *See* Appendices, page 6.
[2] *See* Appendices, page 177.

assurance, the Secretary of State should be prepared to suspend the purchase of silver. In that case it would probably be impossible to provide silver coin to meet the demands of India, and the notes would become inconvertible.

It was suggested that this situation would not last long, since the Indian demand for silver is so important a factor in the silver market that the abstention of the Government of India from purchases would very soon bring about a fall in price. Recent experience, however, has shown that this result is not necessarily produced in all circumstances. For the last six months the Secretary of State has made no purchases of silver, but in spite of his abstention the price has risen to an unprecedented height. We cannot shut our eyes to the possibility that under the influence of an intense demand from China (such as has prevailed recently), or from some other quarter, a considerable period might elapse in which the price of silver might remain beyond the reach of the Government of India.

It was suggested also that the inconvertibility might be partial; that is to say, that the Government of India should take powers to restrict the issue of rupees from the Currency Offices and should issue them only under such conditions as they might think advisable. Some of the practical inconveniences of complete inconvertibility might be avoided in this way, but there would be difficulties in the administration of such a system, and we do not think that in its effect on the credit of the Government and on popular confidence in the note issue it would differ greatly from complete inconvertibility.

The evidence submitted to us was strongly opposed to allowing the note issue in India to become inconvertible, whether wholly or partially, if it can possibly be avoided. It is true that as a result of the war the paper currency has become practically, if not legally, inconvertible in many countries, including the United Kingdom. In Egypt, for instance, where the currency position was affected by influences in some respects similar to those that operated in India, the note issue has been inconvertible since August 1914, and the change was accomplished without difficulty. We believe, however, that the note-using habit is not yet sufficiently established in India to render the introduction of a similar measure there possible without grave risks. Until recently the circulation of notes outside the larger towns was comparatively small, and only two years have passed since notes of small denomination have been introduced. In many parts of the country the climate is not suitable for the use of paper money, and the preference for coin will probably prevail among the mass of the population for many years. In these circumstances a failure to maintain convertibility may be expected to lead to a considerable discount on the note, the extent of which cannot be predicted with any accuracy. The credit of the Government would suffer a severe blow, and if belief in the convertibility of the note were once shaken it might take many years of anxious labour to restore confidence, while the set-back to the development

of a sound and economical monetary circulation in India would be disastrous.

We hold, therefore, that the maintenance of the convertibility of the note issue is a vital part of the Indian currency system.

PRICE OF SILVER.

42. Factors influencing future price of silver.—We have in paragraphs 15—19 traced the causes of the rise in the price of silver. The enquiry conducted by Professors Cullis and Carpenter suggests that on the restoration of order in Mexico the pre-war figures of production will again be reached, and that it is possible that the increasing world demand for the base metals with which silver is associated as a by-product, together with improvements in the method of extraction and the stimulus of high prices, may at an early date lead to a considerable increase in production. On the other hand, the evidence suggests that the demand for silver is likely to continue for a few years on a large scale. The general rise in prices creates a demand for increased supplies of subsidiary silver coinage throughout the world, and though the high price of silver may tend to reduce the demand for the arts, it is difficult to say whether the reduction will be on a sufficient scale to influence appreciably the price of the metal. We have been unable to obtain any reliable evidence regarding the probable demand from China in the near future. As we have stated, China has already imported sufficient silver to counterbalance her exports during the war, but she is still buying, and it is impossible to foresee how long her demand is likely to continue. It would be rash, therefore, to formulate any definite conclusion as to the level at which the price of silver is likely to stand.

43. There are, however, certain considerations which must be taken into account. The Pittman Act imposes on the United States Government the obligation of replacing the silver taken from their reserves, and lays down that until this silver has been replaced they must buy for this purpose at the price of one dollar per fine ounce any silver "of the product of mines situated in the United States, and of reduction works so located" which is tendered to them for purchase. As this replacement will involve the acquisition of considerably more than a year's total production of silver on the present basis of output, while the world's demand for silver is likely to remain high, the process of replacement cannot be completed for some years. During the interval the price of silver cannot be expected to fall below one dollar per fine ounce. Even when the dollar-sterling exchange returns to par, it will be impossible to mint rupees without loss from silver purchased at this price unless the exchange value of the rupee is fixed at 1*s.* 6*d.* or some higher figure.

It is more difficult to form any conclusion as to the maximum beyond which the price of silver is unlikely to rise. When the exchanges are at par, the prices of silver at which the principal silver coinages of the more important countries have a bullion value equi-

valent to their nominal value, are as follows:—England, 66*d.*; France (5 franc piece), 60¾*d.*; U.S.A. (dollar), 59¼*d.* If the price of silver were to remain for any long period at a level substantially over that corresponding to the above figures, it would threaten the silver coinages of France and the United States with the risk of depletion by melting and export, and would also offer inducements to these countries to convert their silver reserves into gold at a favourable rate. In support of this view, we may refer to the recent announcement that the American Treasury has decided to sell to certain American Banks established in the Far East silver obtained by melting the available dollars in their possession (now $55,000,000) at their gold equivalent of 129·29 cents, plus melting, insurance, and shipping charges, whenever that price can be obtained, the intention, presumably, being to prevent silver rising to a point which would lead to the melting down of subsidiary coin. When the price of silver is 137·8 cents per fine ounce, corresponding to 62·9*d.* (gold) per standard ounce, and therefore well above both the French and the American parity, the corresponding bullion value of the silver in the rupee is 1*s.* 11·36*d.* (gold), and the cost of the rupee (including all charges) is approximately 2*s.* (gold). We believe that, if the exchange value of the rupee is fixed at a figure not lower than this, there is substantial ground for holding that the rupee can be established as a token coin, and the maintenance of a satisfactory monetary circulation in India assured.

Effects of a High Rate of Exchange.

44. Our conclusion that a high level of exchange is essential for the establishment of a sound monetary system leads us to a consideration of the more general economic effects of a high rate. Some of the witnesses who have appeared before us have laid great stress on the dangers attending a high level of prices in India, and on the beneficial effect of a high rate of exchange in restraining the rise of prices; others have expressed apprehension as to the effect that a high rate of exchange might have on the well-being of the people of India, the maintenance of Indian trade and the development of Indian industry. We recognise the great importance of the arguments laid before us from these opposite points of view, both in oral evidence and written memoranda, and we now proceed to examine the issues raised by this aspect of the case. This review will lead us to consider the effect of a high rate of exchange on the remittance of funds from India to meet the requirements of the Government.

(a) *Effect on the Level of Prices in India.*

45. Movements of prices in recent years.—At the outset of our enquiry we requested the Government of India to furnish us with up-to-date information regarding price movements in India. The particulars we received in response to our request will be found on pages 159 to 176 in the volume of Appendices to our Report, and we invite attention to the memorandum submitted by the Government of India on the subject.

In illustration of the rise in the price of necessaries of life we cite the following index numbers for the prices of selected articles in 1914, 1915—17, and 1918—19, based on the average wholesale prices for 1900—09 which are taken as the equivalent of 100.

	1914.	1915-17.	1918-19.
Wheat	118	135	180
Country rice	126	122	139
Ghi	132	136	183
Jawar	123	103	236
Bajra	130	123	249
Dal	125	130	166
Raw sugar (gur)	101	134	148
Country salt	111	214	413
Cotton piece goods (Indian made)	109	94	164
Cotton piece goods (imported)	112	138	206

The following table exhibits the rise in Indian prices since 1910, this year being taken as the basic year for the preparation of the table:—

*Index Numbers of Prices in India.**

Year.	Special Index Number for Food Grains (Retail Prices). Column 1.	Special Index Number for imported Articles (Wholesale Prices). Column 2.	Special Index Number for Articles exported (mostly Wholesale Prices). Column 3.	General Index Number for the Articles covered by Columns 2 and 3. Column 4.
1910	100	100	100	100
1911	96	104	107	106
1912	112	107	114	112
1913	118	107	121	117
1914	132	105	126	120
1915	130	134	122	125
1916	120	217	128	151
1917	120	240	134	161
1918	161	265	157	184

* This table is based on the statistics contained in Appendix III to Sir Lionel Abrahams' Memo. B. (Evidence, page 89).

The Index numbers are based on the prices of the following articles at selected stations:—

Column 1.—Rice, wheat, jawar, bajra, gram, barley, ragi (retail prices).

Column 2.—Iron, copper, spelter, grey shirting, grey yarn, coloured yarn, sugar, raw silk, coal, kerosene oil, and salt (wholesale prices).

Column 3.—Jawar, bajra, gram, barley, ragi (retail prices); wheat, rice, tea, sugar, ghi, raw hides, raw cotton, raw jute, raw silk, saltpetre, raw wool, castor oil, linseed, rape seed, sesamum, poppy seed, coal, cotton yarn, T cloth, gunny bags, dressed skins, shellac, indigo (wholesale prices).

Column 4.—Articles included in columns 2 and 3.

For comparison with the above we give for the same years corresponding figures deduced from Mr. Sauerbeck's tables for prices in the United Kingdom, which, though based entirely on wholesale prices, may serve to give an indication of the comparative rise in the two countries:—

Year.	Index Numbers of Prices in United Kingdom.	General Index Numbers for the Articles covered by Columns 2 and 3 (*see* Column 4 above).	Year.	Index Numbers of Prices in United Kingdom.	General Index Numbers for the Articles covered by Columns 2 and 3 (*see* Column 4 above).
1910 . .	100	100	1915 . .	139	125
1911 . .	103	106	1916 . .	176	151
1912 . .	110	112	1917 . .	226	161
1913 . .	110	117	1918 . .	249	184
1914 . .	110	120			

46. It will be seen from these tables, and from the more detailed information contained in Appendix XXVIII,* that there has been a great increase in all prices in India in the last few years. The upward movement had begun before the war, but it has continued, and during the last two years its rapidity has greatly increased. The serious and widespread failure of crops in 1918 was in part responsible for the special rise in the price of food-grains in 1918—19; but the general upward movement is mainly due to causes resulting from the war, including the excessive creation of credit and paper currency and restraints upon free commercial intercourse, which have raised prices throughout the world and have been operative in India as well as elsewhere.

The figures show that on the whole the rise of prices in India has not been so great as the rise in the United Kingdom. A similar conclusion would probably be reached if a comparison were made between Indian prices and prices in other countries outside India whose currencies are depreciated. Amongst the various causes, not easily to be disentangled, which have contributed to this result, the one which specially concerns us is the rise in the exchange rate of the rupee. We shall examine later the operation of this cause and the inferences to be drawn from it as to the level of exchange which it is desirable to establish; but in the first place we proceed to examine the economic effects of a rise in prices on the population of India.

47. Effect of rise in prices on population of India.—As India is a country whose export trade is more valuable than her import trade, it might be thought that an increase in prices would be on the whole advantageous to her. This view has been strongly represented by some of our witnesses; whilst others have

* *See* Appendices, page 159.

expressed equally strongly the opinion that any considerable increase in prices is an evil and a danger. In order to decide between these conflicting views, we have endeavoured to examine the effect of rising prices on the main classes of the population.

According to the census of 1911, 217 millions, that is, 72 per cent. of the population of India, are engaged in pasture and agriculture. But this number embraces classes who are differently affected by the rise in prices. Of 167 million cultivators of their own or rented land, those who have a surplus for sale would ordinarily benefit by a rise in the price of the commodities they produce, but even these—and perhaps their position is the most favourable—have had to contend with the large increase in the price of imported articles, notably cotton piece goods and other necessaries of life. Moreover, if, as is often the case, the cultivator has received advances for his maintenance and for seed, repayable in grain after the harvest, any increase in the value of the grain repaid benefits the money-lender and not the cultivator. On the other hand, the agriculturist who has little surplus produce to sell and lives on what he produces, would, in so far as he maintains himself on his own produce, be unaffected by a rise in the price of foodstuffs, and he would have only a small profit to set against the heavy rise in the cost of the articles he has to buy. The numerous class of farm servants and field labourers, estimated in the census of 1911 at over 41 millions, would ordinarily stand to lose by a rise in prices, except in so far as their wages are payable in kind and not in money. The large class of persons with fixed incomes, which would include persons living on rents, Government servants, professional men, and pensioners, have suffered severely from the rise in prices of the commodities they require, and the urban population, who are not producers, may be placed in the same category. Industrial wage-earners, labourers, and domestic servants have, as a result of increased demands of their services during the war, been able to obtain increased wages. But the evidence which we have received suggests that wages generally in India have advanced more slowly than prices, and much suffering is entailed in the course of the adjustment of wages to new price levels.

48. View of Government of India.—The general effect of the rise in prices is summarised in the following passage, which we quote from the Government of India's memorandum:—

"The effect has of course been felt most directly by the poorer classes, but it has reacted on all sections of the community. Complaints on the subject have been universal throughout the country, and it is reported from the districts that in recent months the topic of high prices has engaged the minds of the people at large to the exclusion of every other; they could understand dearness during the war, but cannot understand why prices do not fall now that the war is over; they can account for some of the rise in the price of food-grains by last year's poor monsoon, but they are puzzled by large increases in the prices of their other necessities of life, the

supply of which is not dependent on a good rainfall. There is no longer any room for doubt that the resultant increase in the expense of living due to the high prices of food-grains, as also of other necessaries, such as cloth, kerosene oil, and the hardships which this increase has entailed on the poorer classes and those on fixed incomes, have been a very important factor in promoting unrest and discontent. At the same time the cultivator, who would ordinarily be the first to profit by the high prices of produce, whether food-grains or other raw material such as jute and cotton, has seen his profits disappear owing to the simultaneous rise in the price of other necessities. The wages of manual labour have no doubt been to some extent readjusted, and ultimately the wages of the clerical and other classes of employees will undergo a similar readjustment. But the process of adjustment, however rapid, must inevitably be a painful one, which no amount of administrative palliatives, such as control of distribution, can alleviate."

These views are not a matter of theory alone. Disturbances have actually arisen in various parts of the country from time to time as a result of high prices, and the social and economic discontent to which they give rise is especially serious in a country where the mass of the population is ignorant and uneducated, and inclined to attribute all calamities to the action of the Government. The rise in prices in India has now reached a point at which it is injurious to the country as a whole, and we believe that any measures tending either to reduce prices or to check a further increase would be beneficial to the mass of the population.

49. Effect of rise in exchange on prices.—The exceptional conditions under which trade was conducted in the course of the war make it impossible to arrive at any precise conclusions as to the extent to which the rise in prices has been influenced by the rise in the exchange value of the rupee. Government control over the movement and prices of food-grains in India undoubtedly prevented prices rising to the full extent that might otherwise have been the case. Restrictions on finance and freight also exerted a powerful influence in the same direction. Again, the scarcity in 1918 operated to raise the prices of food-grains to an abnormal height. While these complicated factors make it impossible to estimate in precise terms the effect of the rise in the exchange value of the rupee on Indian prices, we see no reason to doubt that, in accordance with accepted economic theory, Indian prices would, but for the rise in exchange, have been still further enhanced. Taking the case of imported commodities, the sterling price at which the merchant can lay down goods in India is determined by the cost of production and the transport and other charges. If the exchange value of the rupee rises, this sterling cost is represented by a smaller number of rupees, and the goods can be sold at a lower rupee price. Again, in the case of exports such as wheat, whose price outside India is determined by world-wide conditions of production and consumption, the sterling price which can be obtained for a given quantity of wheat will, if exchange rises, be represent-

ed by a smaller number of rupees, and the price which the grower will receive must necessarily be lower.

These considerations do not apply with equal force to exported produce such as jute, of which India enjoys a practical monopoly, since, if exchange rises, the Indian producer has it in his power to exact a larger sterling price in order that he may receive the same number of rupees. But even for such commodities as jute, the power of varying the price to be paid by the consumer is far from absolute, and it is probable that a higher exchange means a somewhat lower price to the producer. Nor do precisely the same considerations apply to products which are grown almost entirely for internal consumption, as, for instance, food-grains such as jawar or bajra. While, however, movements of exchange have little direct effect on the price of such products, it is probable that they have indirect effects which give a result similar in kind though less in degree.

50. High level of exchange advantageous.—We are led therefore to the conclusion that on economic and social grounds it is not desirable to restore a low level of exchange for the rupee under present conditions. Such a level would tend to augment prices generally and to aggravate the dangers of social and economic discontent. Having regard to the conditions under which the large mass of the population lives, we are satisfied that in so far as the rise in exchange has mitigated a rise in Indian prices, it has been to the advantage of the country as a whole, and that it is desirable to secure the continuance of this benefit.

(b) *Effect on Indian Trade.*

51. Influence of high exchange on Indian trade.—We now pass on to consider how far Indian commerce is likely to be affected by the maintenance of the exchange value of the rupee at a high level. We have already referred to the effects of a rise in exchange in stimulating imports and checking exports, and have expressed the opinion that these effects are transitory, and that they are no longer operative when wages and other elements of cost have adapted themselves to the new level of exchange.[1]

Indian trade is at present prosperous, and India is in a favourable position for maintaining this prosperity. The world shortage of raw materials and foodstuffs is likely to ensure a continuing demand for Indian produce during the period necessary for complete adjustment, while the great rise in the level of prices in countries importing from India should generally enable the Indian producer to obtain a satisfactory rupee price for his commodities in spite of the high exchange. It has, moreover, to be remembered that a high exchange brings with it certain counter-balancing advantages

[1] This question was discussed fully in the Report of the Herschell Committee of 1893 (paras. 27 and 116-120). *See also* Memorandum received from the Government of India regarding Indian price movements (Appendices p. 164, § 15).

even to producing interests. It tends, for instance, to keep down the cost of imported stores and machinery as measured in rupees, and, as we have pointed out above, exercises a check on the rising cost of living in India and consequently on the rise in wages.

We do not think it necessary to enter into a detailed review of the conditions under which trade in India's staple products is conducted. Some of these commodities, of which jute is the most important, are virtually monopolies with assured markets, while others, such as tea, cotton, seeds and hides, are articles for which the world demand is insistent despite the high range of prices. Exchange is only one and not necessarily the most important factor of which account has to be taken. After careful consideration of the evidence placed before us we have arrived at the conclusion that Indian trade is not likely to suffer any permanent injury from the fixing of exchange at a high level.

There is one qualification which it is necessary to add to the above statement. It seems probable that prices generally will remain at a high level for a considerable time, and that any return to lower levels will be gradual; but if, contrary to this expectation, a great and rapid fall in world prices were to take place, a new element of disturbance would be introduced. The costs of production in India might fail to adjust themselves with equal rapidity to the lower level of prices, and Indian exports might suffer to an extent which would endanger the maintenance of exchange at the level which we propose. In that case it would be necessary to consider the problem afresh, and take the measures which might be required by the altered circumstances.

(c) *Effect on Indian Industrial Development.*

52. Influence of high exchange on industrial development.—Our attention has been drawn by certain witnesses to the important movement that is now taking place in the development of industry in India, and some apprehension has been expressed lest a high rate of exchange should exercise a retarding influence on this welcome activity. We recognise that competitive imports into India may be temporarily stimulated by the high rate of exchange, especially from countries where the cost of production is low; but even in the period which may elapse before the adjustment of prices and other conditions to the new level is complete, this influence, so far as manufactured articles from Europe and America are concerned, is likely to be counteracted by the greatly increased cost of production in the exporting countries at the present time. Moreover, a high exchange will tend to retain for India the advantage of a low cost for wages and raw materials, and in so far as nascent industries are dependent on imported machinery, plant and stores, they will benefit from the lower rupee prices payable for them. On a review of all the facts, we are of opinion that the development of Indian industry will not be seriously hampered by a high rate of exchange.

(d) *Effect on Home Charges.*

53. Home charges: effect of high rupee.—One of the reasons for the closing of the mints to the free coinage of silver in 1893 was the increasing difficulty experienced by the Government of India in providing for their sterling obligations when the exchange value of the rupee was continuously falling. The fixing of the rupee at 1*s*. 4*d*. materially improved the revenue position and enabled the Indian Treasury to do without the additional taxation that would otherwise have been necessary. A high rate of exchange would result in further advantages in this direction. When the exchange value of the rupee was 1*s*. 4*d*. the rupee equivalent of the Home charges on the basis of 25,000,000*l*. a year was $37\frac{1}{2}$ crores; while, if the necessary sum were remitted at an exchange of 2*s*., the cost would be 25 crores only, a saving of $12\frac{1}{2}$ crores.

On the other hand there would be a loss involved in the revaluation in rupees of the sterling investments and the gold in the Paper Currency Reserve.

If the revaluation were made at 2*s*. to the rupee, the depreciation to be made good would amount to 38·4 crores. If the whole of the revenue saved in respect of the Home charges could be employed for the purpose of meeting this loss it would be recouped in about three years. Thereafter a considerable surplus revenue would remain which might be employed in furthering the development of India or in the reduction of taxation.

This is an incidental advantage in fixing a high rate of exchange which must be taken into consideration.

54. Conclusion as to effect of high rupee.—We are thus led to the conclusion that the material interests of India are not likely to suffer from the fixing of a high rate of exchange for the rupee, and that certain important advantages will follow from such a course of action. The question now arises as to the manner in which the exchange should be fixed.

SHOULD THE RUPEE BE FIXED IN RELATION TO GOLD OR STERLING?

55. Before the war the convertibility of sterling into gold was complete. Sovereigns and half-sovereigns were in circulation, and Bank of England notes and other bank notes which were in use in the United Kingdom could be exchanged without any difficulty for gold. It was therefore unnecessary in considering the problems of Indian exchange to make any distinction between the two. At the present time, however, gold coin is no longer in circulation in the United Kingdom, and Treasury notes, which form the great bulk of the full legal tender currency, are not in practice convertible into gold. The result is that there is a divergence between the value of the pound sterling and the sovereign. One hundred ounces of fine gold can be coined into 425 sovereigns; but at the quotation on 17th December (108*s*. 9*d*. per oz.) 100 ounces of fine gold cost approximately 544*l*. in sterling, *i.e.*, in notes. Thus 1*l*.

sterling (paper) is equivalent to $\frac{426}{544}$, or ·78 of the sovereign (gold), a discount of 22 per cent.; or, conversely, the sovereign (gold) is worth $\frac{4}{5}$ *l*., or 1·28*l*. sterling (paper), a premium of 28 per cent.

A corresponding depreciation is shown in the exchange between sterling and the American dollar, which is convertible into gold. The gold sovereign is equivalent to $4·8666, while the pound sterling was quoted on 17th December at $3·83, a depreciation of over 21 per cent.

It therefore becomes necessary to consider whether, if the rupee is to be stabilised, its fixed relation should be with sterling, as hitherto, or with gold. In the latter case the necessary result will be that, until the gold basis of the British currency is restored and sterling becomes equivalent to gold again, the rupee-sterling exchange will fluctuate in the same manner as the dollar-sterling exchange. This issue was brought into prominence by Mr. Lucas, Financial Secretary at the India Office, who in his written memoranda and oral evidence has argued the case for a fixed relation with gold with much force and ability. We have given anxious consideration to this question, and our unanimous conclusion is that, for the reasons which we proceed to state, the balance of advantage lies in fixing the relation of the rupee with gold rather than with sterling.

56. Advantages of fixing in sterling.—The main inducement for retaining the fixed relation with sterling is that a larger part of the trade of India is with sterling-using countries than with countries upon an effective gold basis. The only important countries to be placed at present in the latter class are the United States and probably Japan. The exports to these two countries in 1918—19 amounted to 25 per cent. of the total exports of India (as compared with 14 per cent. before the war), while the import trade from them was 30 per cent. of the total (as compared with 5 per cent. before the war). On the other hand, the trade with the British Empire (excluding those portions which do not use sterling) amounted to 40 per cent. for exports and 48 per cent. for imports. It is argued that the advantage of fixity of exchange should be retained for the most important section of India's trade; and also that, in the interests of the Empire as a whole, it is desirable that the exchange system should be such as to facilitate and promote trade within the Empire rather than outside it, and, we may add, to retain for centres within the British Empire the finance of Indian trade.

This consideration has undoubtedly some weight, especially as the effect of war conditions has already been to divert to Japan and the United States a part of the trade formerly exchanged with the United Kingdom and other European countries. We do not, however, consider that a fluctuating sterling exchange will create an obstacle of a serious character to trade between the United Kingdom and India or to existing methods of financing that trade, provided that the system in force is such as to enable trade requirements for remittance to be met readily and to their full amount.

In any case the fluctuations of the rupee-sterling exchange will only exist until the gold basis of the British currency is restored.

57. Advantages of fixing in gold.—The advantages, on the other hand, of fixing the exchange value of the rupee in relation to gold may be stated as follows:—

(i) Great and admitted inconveniences attach to a currency which is depreciated and may suffer further depreciation. If India's currency is linked to sterling it will share those inconveniences. Her position as an exporting country with a favourable trade balance enables her to avoid them by linking her currency to gold.

(ii) We have already stated our conclusion that it is desirable to stabilise the rupee at as early a date as practicable at a level which will ensure that it remains a token coin, and will remove the necessity for further increases in its value to meet further rises in the sterling price of silver. We have also pointed out that such rises might result from further depreciation of sterling. This possibility increases very seriously the difficulty of fixing a sterling value for the rupee which could be maintained with certainty; but if the value of the rupee is fixed in relation to gold and not to sterling, one disturbing cause at least is eliminated, since any rise in the sterling price of silver resulting from further depreciation in sterling would be counterbalanced by a similar automatic rise in the sterling value of the rupee.

(iii) The value which it would be necessary to fix in sterling at the present time, in order that the rupee might have an exchange value exceeding that of its silver content, would be a high one. Under present conditions we do not, as we have explained, regard that as a disadvantage. But if at some future time sterling recovers its value and becomes equivalent once more to gold, the sterling value for the rupee imposed by present conditions might be found too high, since that value would have increased in relation to gold, and probably in relation to other commodities, in proportion to the recovery of sterling from its depreciation. It may be answered that if the value is found to be too high, it can be reduced. But any reduction of the value fixed would have to be made by the Legislature or by acts of the Executive, similar in character to those which have enforced successive rises in value, but arbitrary because not dictated by circumstances and therefore specially injurious to commercial confidence. If, on the other hand, the value is fixed in relation to gold, it can be fixed with safety at a lower figure and although at the present time the corresponding sterling value of the rupee will be no less high than if it had been fixed in sterling, the sterling equivalent will automatically fall

in correspondence to any recovery in sterling, and will ultimately coincide with the gold value.

(iv) If the relation of the rupee to sterling is fixed, while sterling varies in relation to gold, it is evident that the relation of the rupee to gold will vary. But if (as we think essential) the rupee and the sovereign are both to remain unlimited legal tender in India, and to be available for circulation, it is necessary that the relation of the rupee to the sovereign should be fixed, since two coins cannot remain in circulation as unlimited legal tender and at the same time stand in a variable relation to one another. The result would be that the relation of the sovereign to gold would vary—in fact, that the sovereign would become a token coin in India, divorced from its bullion value, and rated at a fixed number of rupees. It would follow that the import of sovereigns by the public must be prohibited, that the danger of smuggling and illicit coining must be incurred, and that gold coin and bullion would not be interchangeable.

(v) In paragraphs 65—67 we state our view that it is very desirable to permit the free export and import of gold bullion and coin, and to issue gold coin in India for an equal weight of gold bullion subject only to an appropriate coinage charge. It is clear from what we have said above that these objects can be attained in the near future if the rupee stands in a fixed relation to gold, but not otherwise.

Balance of advantage on side of fixing in gold.—The balance of advantage appears to us for these reasons to be decidedly on the side of fixing the exchange value of the rupee in terms of gold.

POSTPONEMENT OF DECISION UNDESIRABLE.

58. Reasons against postponing decision.—We have now dealt with the various aspects of the question which it was necessary to examine, and we are in a position to formulate our definite recommendations as to the course to be pursued; but before doing so we must give our reasons for not accepting the view, which has been pressed upon us, that no attempt should be made at the present time to fix any definite or final figure for the relation between the rupee and either gold or sterling, but that the policy followed since 1917 should still be pursued. For the development of this view and the explanation of the practical steps which would give effect to it, we must refer to the very able evidence of Sir Lionel Abrahams.

It is true, as we readily admit, that present circumstances are abnormal, and that it is extremely difficult to foresee future developments. This has been demonstrated by the changes in the situation which have taken place since our inquiry began, and this fact

was advanced as a reason for recommending that policy should wait upon events, that the exchange value of the rupee should be raised, if a further increase in the price of silver required it, and that it should again be lowered if events proved that the level reached was inconveniently high. But in our terms of reference we are directed to make recommendations with a view "to ensuring a stable gold exchange standard," and we do not think that it would be an adequate discharge of our responsibilities to submit proposals which did not aim at securing stability in the near future, if, as we believe, such a result is attainable. The postponement of a decision which is synonymous with the continuance of the existing uncertainty would be open to serious criticism, and would entail the prolongation of Government control over exchange and over the import of the precious metals into India.

THE RATE RECOMMENDED.

59. Establishment of a stable relation between the rupee and gold at the rate of ten rupees to one sovereign reccommended.—We have now arrived at the following conclusions:—

(i) The object should be to restore stability to the rupee, and to re-establish the automatic working of the currency system at as early a date as practicable (para. 36).

(ii) The stable relation to be established should be with gold and not with sterling (para. 57).

(iii) The gold equivalent of the rupee should be sufficiently high to give assurance, so far as is practicable, that the rupee, while retaining its present weight and fineness, will remain a token coin, or in other words, that the bullion value of the silver it contains will not exceed its exchange value (para. 43).

After most careful consideration we are unanimous (with the exception of one of our members, who signs a separate report) in recommending that the stable relation to be established between the rupee and gold should be at the rate of ten rupees to one sovereign, or in other words, at the rate of one rupee to 11·30016 grains of fine gold both for foreign exchange and for internal circulation. While some of our number would have preferred that the rate to be adopted should be nearer to that which has been in force for the last 20 years, we all recognise that no lower rate will attain the objects which we find to be indispensable. Our recommendation accords with the views expressed by the Government of India[1] after they had taken account of the changes in the situation since the preparation of their original proposals. They strongly support the establishment of a fixed relation between the rupee and gold, and the adoption of the rate of ten rupees to one sovereign, and they express the view that this solution "combines

[1] *See* Appendices, page 177.

a more real stability with maximum possible assurance of convertibility, and has, in fact, all the elements of a completely satisfactory permanent system."

We believe, as we have already stated (para. 43), that strong forces will come into operation to prevent the price of silver rising to a point which will cause the bullion value of the rupee to exceed 2s. (gold). If, however, contrary to our expectation, the price of silver should rise for more than a brief period of such a point, the situation should be met by all other available means rather than by impairing the convertibility of the note issue. In the event of such a rise in the price of silver, the Government might diminish the demands upon them for currency by reducing as far as possible the sale of Council Bills, relying on the free import of gold and silver, which we recommend, to provide alternative means of remittance. They would naturally endeavour to meet the demands for metallic currency by the use of gold, and abstain as far as possible from purchasing silver. If, in their judgment, it should be absolutely necessary to purchase silver, they should be prepared to purchase even at a price such that rupees would be coined at a loss.

The principal steps for giving effect to our recommendation are (1) a notification changing the present acquisition rate for imported gold and fixing it at the rate of Rs. 10 to the sovereign, (2) an amendment of the Indian Paper Currency Act and Indian Coinage Act, so as to make the sovereign legal tender for Rs. 10 instead of for Rs. 15, and (3) the withdrawal of the existing undertaking to give Rs. 15 for a sovereign.

In this connection it is necessary to consider whether an opportunity should be given to holders of sovereigns to present them for exchange at the existing rate at the time of the introduction of the new ratio (*see* para. 69 below).

Other steps necessary as regards—

(1) sales of Council Drafts and Reverse Councils;

(2) import and export of gold and silver;

(3) coinage;

and also as regards the Paper Currency Reserve and the Gold Standard Reserve, are dealt with in the appropriate paragraphs of this Report.

60. Replies to possible objections.—Two objections have been raised to the course which we recommend:—

(i) It is suggested that if the sovereign, or the weight of gold in a sovereign, is obtainable for Rs. 10 instead of Rs. 15, or an even larger number, Indians will regard gold as exceptionally cheap, and will absorb greatly increased quantities. It is possible that the Indian demand may, to some extent, be diverted from silver to gold; but in the present conditions of the supply of the two metals, and the demand for them, we do not regard this neces-

sarily as an evil. At the same time, we emphasise the necessity for using all possible means for encouraging the people of India to employ their savings in more useful and fruitful ways than in the acquisition of precious metal, whether gold or silver.

(ii) It is urged that the existing ratio between gold and silver in India is sanctioned by the law and has been in existence for a considerable period, and that to disturb it will be contrary to sound policy. We only agree in this argument to the extent that the legally established ratio ought not to be modified lightly or on insufficient grounds. The modification is, however, clearly within the competence of the legislature, and if it is necessary in order to remove the grave evils of the present position and to re-establish a sound and automatic currency system, we think it is undoubtedly justified. We believe that it is open to far less objection than any of the other alternative courses that have been suggested.

Remittance to and from India: Council Drafts and Reverse Councils.

61. Extent to which Council Drafts should be sold.—We now proceed to consider questions connected with the system of remittance to and from India.

We agree with the Chamberlain Commission in holding that Council Drafts are sold not for the convenience of trade, but to provide the funds needed in London to meet the requirements of the Secretary of State on India's behalf in the widest sense of the term. There is, in our opinion, no obligation to sell drafts to meet all trade demands. If our proposals in paragraphs 65 to 67 regarding the free import of gold into India and the maintenance of a gold mint are adopted, the way will be open for the settlement of trade balances by means which are independent of the sale of Council Drafts. India, however, normally enjoys a large favourable balance of trade, and the adjustment of this balance mainly by the import of gold would probably involve the shipment to India of more gold than is actually required for absorption by the public. If, therefore, without inconvenience or with advantage the Secretary of State is in a position to sell drafts in excess of his immediate requirements when a trade demand for them exists, we see no objection to his doing so, provided that due regard is had to the proper location of the reserves, to which we refer later. Such sales would tend to economise the movements of gold, and would provide additional facilities for telegraphic remittance, which is an advantage to trade.

The above observations apply to normal times when the purchase of silver for coinage can be readily effected. So long as the existing difficulties continue it will be advisable to adhere to the system at present in force, according to which the actual amounts of Coun-

cil Drafts sold weekly are fixed with reference to the Secretary of State's requirements and the capacity of the Government of India to meet them.

Minimum rate.—While sterling continues to be divorced from gold, the fixing of the rupee in terms of gold will involve fluctuations in its sterling equivalent; and the minimum rate for Council Drafts will be fixed from time to time on the basis of the sterling cost of shipping gold to India. When sterling is again equivalent to gold, the minimum rate will remain fixed and the price obtained for Council Drafts will vary between the gold points according to the demand.

62. Reverse Councils; should be readily available and include telegraphic transfers.—The Chamberlain Commission recommended that the Government of India should make a public notification of their intention to sell in India bills on London at a price corresponding to the gold export point, whenever they were asked to do so, to the full extent of their resources. We agree entirely with this recommendation. We are informed that inconvenience has resulted in the past from the necessity of consulting the Secretary of State before offers of reverse remittance were announced, and to ensure public confidence in the system it is desirable that the authorities in India should be in a position to take action without the delay involved by reference to London. We are also informed that facilities for telegraphic remittance, which were first offered in connection with the sales at the outbreak of the war, were greatly appreciated by the commercial community in India. We, therefore, recommend that the Government of India should be authorised to announce, without previous reference to the Secretary of State on each occasion, their readiness to sell weekly a stated amount of Reverse Councils (including telegraphic transfers) during periods of exchange weakness. The rate will, as in the past, be based on the cost of shipping gold from India to the United Kingdom. So long as sterling is divorced from gold, it will not be possible to announce a fixed rate at which sales will uniformly be made, but the Government of India should be prepared to quote the appropriate figure as soon as the demand for remittance from India makes itself apparent. During this period, assuming that our recommendations regarding the exchange value of the rupee are adopted, 10 rupees will purchase the sterling equivalent of one sovereign less a percentage to cover the charges of remittance.

INDIAN DEMAND FOR PRECIOUS METALS.

63. Character and extent of Indian demand for gold.—We now turn to the policy that should be adopted in regard to the import and export of the precious metals into and from India.

Statistics regarding the imports of gold into India on private account in recent years are shown in paragraph 14. It will be

seen that during the five years preceding the war, India's average annual import of gold coin and bullion exceeded 19,000,000*l*.

It has frequently been alleged that an undue proportion of the world's gold supply is absorbed by India. It must be remembered, however, that the population of India exceeds 315 millions, and that the use of gold (or, alternatively, of silver) plays an important part in social ceremonies sanctioned by religion and tradition. Presents of gold or silver ornaments are obligatory at weddings and on other ceremonial occasions; and this custom is supported by the practical consideration that a woman, whether Hindu or Moslem, who possesses gold and silver ornaments, or coins converted into ornaments, is entitled to hold them as her personal property. It has also always been the habit in India to use the precious metals as a store of value, and to hold savings in this form; nor, until banking and investment facilities have been extended, and the habit of using them has been acquired by the people of India, is it easy to see in what other form savings can be accumulated. We do not, therefore, consider that the quantity of gold taken by India for all purposes in the period before the war was disproportionately large in relation to her economic condition, and it must be assumed that so long as existing conditions prevail India will continue to require a considerable quantity of gold for the purposes named above.

64. We have previously pointed out that the normal balance of trade makes India a creditor country, and as such she is entitled to require payment for her produce in the form most acceptable to her people. Indeed, India's capacity to draw gold from other countries depends in the last resort on the desire of her customers to secure her produce, and, so long as they continue to take it, India will be in a position to demand gold, in so far as she may prefer payment in this form to the import of commodities or the investment in foreign securities of credits due to her.

We do not wish, however, by these remarks to lend support to any suggestion that the import of precious metals is the most advantageous way by which India can adjust her claims against other countries. The accumulation of stores of gold and silver is an unprofitable method of saving, and it would undoubtedly be to India's own interest, and to the interests of the world at large, for her to employ her wealth in productive directions. We are, therefore, glad to learn that an increasing interest is now being shown by Indians in the promotion of industrial enterprise, and we consider (*see* para. 73) that facilities for the deposit and investment of savings should be increased in all practicable ways. This may tend ultimately to reduce India's demand for the precious metals.

Import and Export of Gold.

65. Free import and export of gold advocated. —Under the Gold Import Act all gold imported into India has to be tendered to Government at a specified rate based on the exchange

value of the rupee and the premium on gold. The export of gold is not prohibited, but owing to the fact that gold commands a substantial premium in the Indian bazaar there is no tendency for it to leave the country under existing conditions. The provisions regarding the import of gold were avowedly enacted under the stress of war and were only intended to be temporary. It is, in our opinion, desirable that the entry of gold into India should be freed from regulation or control by the Government. We accordingly recommend that the Gold Import Act should be repealed as soon as the change in the statutory ratio of the rupee to the sovereign, to which we refer below, has been effected. Movements of gold to and from India would of course continue, as in the past, to be reported for registration and statistical purposes.

Gold as Currency.

66. Use of gold as currency.—The fixation of the rupee in terms of gold and the disappearance of the internal premium on gold due to the removal of the prohibition on import will again enable gold to circulate as currency. It is, therefore, necessary to consider how far the extended use of gold currency is desirable in India. We agree in principle with the recommendations of the Chamberlain Commission in this connection, but the position has changed in certain respects since the issue of their report, and some modifications in the policy suggested are advisable. We agree with their conclusions that the Government should continue to aim at giving the people the form of currency which they demand, whether rupees, notes, or gold, that the use of the note should be encouraged, that the currency most generally suitable for the internal needs of India consists of rupees and notes, and that it would not be to India's advantage actively to encourage the increased use of gold in the internal circulation. We also share the view that gold can be more advantageously employed in the Government reserves, where it is available for meeting demands for foreign remittance, than in the hands of the people in the form of currency. For some time, however, it may be difficult to meet all demands for metallic currency in rupees, and a more extensive use of gold may be necessary to ensure confidence in the note issue. We understand that on recent occasions the issue of gold coin by the Government has been looked upon in certain parts of India as an indication that the Government were in difficulties regarding the provision of metallic currency. In order to avoid creating this impression by exceptional issues, we think that so long as the purchase of adequate supplies of silver continues to be difficult it would be advisable for the Government, as one of the normal methods for meeting demands for currency, to issue gold coin in moderate quantities. When the supply of silver has ceased to be difficult, the necessity for the issue of gold coin will diminish, but it is probable that there will always be a demand for gold in certain parts of India. We consider, therefore, that the Government of India should maintain their pre-war practice of making gold coin available when it is demanded by the publc.

67. Facilities for minting sovereigns in India and refining gold recommended.—In order that gold currency may be available when required it is important to provide facilities in India for the conversion of gold bullion into legal tender coin. These facilities might be given by the establishment of an Indian gold mint, which would mint Indian gold coins such as the gold mohur, or by the reopening of the branch of the Royal Mint in Bombay. After careful consideration we have come to the conclusion that it will be more advantageous to India to continue to use the form of gold currency to which she has become accustomed and which, on account of its wide circulation, is a universally recognised medium for the settlement of external obligations. We therefore recommend that the branch of the Royal Mint which was opened in Bombay during the war for the coinage of sovereigns and half-sovereigns and has since been temporarily closed, should be reopened, and that arrangements similar to those in force in the United Kingdom should be made for the receipt of gold bullion from the public for coinage. The Government of India should announce its readiness to receive gold bullion from the public, whether refined or not, and to issue gold coin in exchange at the rate of one sovereign for 113·0016 grains of fine gold, subject to a small coinage charge. This undertaking would not of course require the constant operation of the gold mint, if the demand for the coinage of gold did not justify it. The issue of gold coin in exchange for unrefined gold makes a gold refinery necessary. If the need is not met by private enterprise, we recommend that facilities should be given to the public by which they may be able to have gold refined at the Government refinery on payment of charges sufficient to cover the cost of the operation.

68. Withdrawal of obligation to give rupees for sovereigns recommended.—Sovereigns and half-sovereigns have been for many years legal tender in India, and, as we have stated in paragraph 6, the Government of India have undertaken by notification to issue rupees in exchange for sovereigns presented to them. In normal times, and whenever the supplies of silver permit, the Government of India will doubtless offer all facilities for the conversion of legal tender gold into legal tender silver coin and *vice versâ;* but, in view of the present shortage of silver, we consider that the obligation to give rupees for sovereigns should be withdrawn.

69. Protection of existing holders of sovereigns and gold mohurs against loss from change of ratio.—Under the scheme we have advocated the gold content of the sovereign will be exchangeable in India for Rs. 10, and in order to put this rate in force it will be necessary to amend the statutes under which the sovereign is rated at Rs. 15, and to reduce the rate to Rs. 10. It will also be necessary to cancel the notification under which the Government have undertaken to give Rs. 15 for all sovereigns tendered at the Reserve Treasuries. The question thus arises as to the treatment that should be accorded to the present

holders of sovereigns in India. It is undoubtedly open to the Government to enact through the competent legislature that the rate at which the sovereign is legal tender should be reduced from Rs. 15 to Rs. 10 and to cancel the notification to which we have referred. We do not recognise any legal obligation on the part of the Government to indemnify holders of sovereigns from loss through change of rate, but we think that reasonable opportunities should be given to the public to exchange sovereigns in their possession at the rate of Rs. 15 at the time of the introduction of the new ratio. In order to reduce the period of transition, which must necessarily be attended by obvious risks and inconveniences, the offer should run for a short period only, and if the impending change is widely notified and opportunities for the tender of sovereigns are made available at a large number of places (which would include all Treasuries and possibly all Sub-Treasuries), we hope that it may be found practicable to limit the period to a calendar month. The period suggested is short, and its precise duration should be determined on the discretion of the Government of India; but we feel strongly that action, when taken, should be prompt. In order to prevent an excessive call upon their resources of silver, the Government should reserve to themselves the option of redeeming sovereigns in gold coin at the rate corresponding to the new ratio (*viz.*, $1\frac{1}{2}$ sovereigns for each sovereign), to be payable after the termination of the period of redemption, and to be represented in the meantime by certificates or other suitable instruments created for the purpose.

There would be advantages in carrying out this operation at an early date so that the imports of gold coin and bullion into India may be free from control, and that the sovereign may be put into circulation as the equivalent of Rs. 10. But it must be for the Government to determine the detailed steps by which effect should be given to our suggestions.

The gold mohurs which were coined and issued during the war as the equivalent of 15 rupees should also be redeemed at that rate either now or at some later period as may be convenient. After a reasonable opportunity for redemption has been given, any remaining unredeemed should be demonetised.

Import and Export of Silver.

70. Removal of prohibition of import of silver recommended.—We have already indicated that we are in favour of the removal of Government intervention in the free flow of the precious metals to and from India as soon as practicable. The import of silver was prohibited at a time of abnormal demand for currency and limitation of supply with the object of preventing private buyers in India from competing in the silver market with the Secretary of State. It is difficult to estimate how far the removal of their competition has facilitated the silver purchases of the Secretary of State during the last two years. The evidence we have taken suggests that, in

spite of the prohibition of the melting of silver coin, the melting of rupees has taken place on a large scale. When the bullion value of the rupee approximates closely to its exchange value the most economical method of obtaining silver in India is by melting coin. In so far as the demand for silver for social and industrial purposes, enhanced by the scarcity of gold, has been met in this way, the effect of the prohibition of private imports was to increase the amount of silver which the Secretary of State had to purchase. If the restrictions on gold are removed the demand for silver may be expected to decrease, but a considerable quantity will always be required for social and industrial purposes. We consider that the disadvantages of meeting the public demand through Government agency by the indirect and expensive method of issuing additional currency, outweighs any advantage which may be gained in respect of the Secretary of State's purchases. We therefore recommend the removal of the prohibition on the import of silver as soon as is convenient.

71. Removal of import duty on silver recommended.—Prior to the year 1910 silver bullion and coin other than current coin of the Government of India were included in the general tariff schedule of articles liable to an import duty of 5 per cent. *ad valorem*. In that year it was necessary to raise additional taxation, and it was decided that silver was a luxury article on which an additional import duty might suitably be imposed. The rate was accordingly raised to four annas per ounce. At that time the price of silver was such that the additional duty on silver could have no influence on the currency system, but the rise in the price of silver to a height at which the bullion value of the rupee approximates to its exchange value introduces fresh considerations; for whenever the exchange value of the rupee does not exceed the bullion value by the amount of the duty, it is cheaper to obtain silver for the arts in India by melting the currency than by importing silver bullion. So long, therefore, as the divergence between the bullion value and the exchange value of the rupee is not large, the retention of the import duty may throw upon the Government of India the burden of providing rupees in excess of the needs for currency purposes. The removal of the duty has also been advocated on the ground that it imposes an unfair burden on the poorer classes, to whom a certain quantity of ornaments is a social necessity rather than a luxury. We do not attach weight to this argument, but we believe that there is a strong feeling in India against the retention of the duty in that it is an obstacle to the establishment of a world market for silver in Bombay, and places the Indian consumer of silver at a disadvantage in comparison with that of the population of other countries. The Government of India would prefer to defer consideration of the removal of the duty until the results of the relaxation of the control over the movement of the precious metals have been observed,[1] but we see no reason for the postponement of the decision on the point of principle involved. Since the prohibition of the import of silver, the revenues of the Government of India

[1] *See* Appendices, page 179, paragraph 7.

have been deprived of the yield from the silver duty, which was about one crore annually before the war, and the gap has been filled from other sources. The abolition of the duty at the present time would therefore involve no readjustment of the burden of taxation. For these reasons we recommend that when the prohibition of import of silver is removed, the duty should also be removed, unless in the opinion of the Government of India the fiscal position demands its retention.

72. Retention of control over export of silver for the present recommended.—As regards the export of silver, we are unable to recommend the removal of the prohibition at present, although we think that the removal of all restrictions is an ideal to be attained as soon as circumstances permit. As long as the bullion value of the rupee is near its exchange value, it is possible that the export of silver rupees or silver obtained by melting rupees will be a profitable transaction, and it is necessary that Government should be in a position to protect the currency from depletion by export. We recommend, therefore, that the export of silver, except under licence, should be prohibited, until changed conditions again definitely establish the rupee as an over-valued token coin. Meanwhile it is important that the production of silver in India should not be discouraged by a measure which is intended only to protect the currency. We understand that silver mined in India is now purchased by the Government of India at rates fixed by contract with the producers. We hope that so long as the Government of India require silver this arrangement will be continued on suitable terms; but if at any time before the removal of the export prohibition the continuance of the purchase by Government of silver mined in India should be unnecessary or impracticable, we consider that the producers should be permitted to export freely under licence the silver produced from their mines.

Facilities for Saving and Investment.

73. Increased opportunities for saving and investment recommended.—We have already referred to the extensive use in India of the precious metals, mainly in the form of currency, as a store of value. It has been urged that this practice is largely due to the inadequacy of the facilities for the disposal of savings in a manner which will enable them to be used productively. We, therefore, welcome the recent announcement of the Government of India that a feature of the scheme for the amalgamation of the Presidency Banks is the opening of at least 100 new branches within the next five years. We recommend that this policy should be actively pursued. By the extension of the activities of the amalgamated Presidency Banks and other sound banking institutions in India, we hope that facilities for the deposit of savings will gradually be made available in all headquarters of administrative districts and other towns where no banks have yet been established. We suggest also that the Government of India

should consider whether it is practicable to abolish the existing stamp duty on cheques.

An extension of banking facilities, however, on such a scale as would attract deposits from the remoter areas is unlikely in the near future, and we think, therefore, that the rural population should be encouraged to take fuller advantage of the opportunities for making interest-bearing deposits in Co-operative Credit Societies and the Post Office Savings Banks. We are impressed by the comparatively insignificant figure of the total deposits in the Post Office Savings Banks, amounting to only Rs. 24½ crores on 31st July 1914, before the conditions that ensued on the outbreak of war led to the heavy withdrawals referred to in paragraph 9. We understand that the substantial increase in deposits in the years 1912—13 and 1913—14, amounting to over four crores, was due mainly to the grant of additional facilities, and we recommend that the Government of India should examine how far, notwithstanding the admitted administrative difficulties, it may be possible to improve the present procedure for the deposit and withdrawal of money, and to increase the number of post offices conducting savings bank business.

In addition, we advise that all possible facilities should be made available for the investment of savings in Government Loans. In particular, in view of the success which has attended the Government of India's war borrowings through the Post Office, notably in the form of cash certificates, we suggest that a Postal Section should be retained as part of the normal borrowing system of India.

It has been suggested to us that Indian investors would be prepared to purchase sterling securities of the Indian Government if facilities were given for the purpose. We are not in a position to judge how far this proposal is practicable or expedient, but we desire to bring it to the notice of the Secretary of State and the Government of India.

Purchase of Silver for Coinage.

74. Silver purchases.—Before leaving the subject of the precious metals, it will be convenient to deal with the criticisms of certain witnesses regarding the conditions under which purchases of silver for coinage have been made. The allegations of the critics are to the effect that the method of purchase through a broker, mainly in the London market, is unsatisfactory, and has resulted in purchases being made at an unnecessarily high price; and that purchases by open tender in India would give better results. We have considered the subject carefully, and without entering into unnecessary details, we are satisfied that the purchases of the Secretary of State, which are made in the same manner as the purchases of His Majesty's Mint, many foreign Governments, and the banks concerned in the supply of silver to the Far East, are suitably conducted. We do not, therefore, make any recommendation for modifying the present practice, though we have no wish to suggest any limitation of the freedom which the Secretary of State now enjoys of making

purchases in India or elsewhere than in the United Kingdom should he think it advantageous to do so.

Paper Currency Reserve.

75. Principles underlying recommendations regarding note issue.—In paragraph 28 we have referred to the large expansion of the note-issue during the war. This expansion has been in great part due to special causes arising from the war; but we believe that it has been beneficial to India, and we should welcome any further action that might tend to foster the note-using habit, especially under present conditions when the purchase of silver for coinage is attended with serious difficulty. But the continued popularity of the note can only be assured if its convertibility is guaranteed beyond all possible doubt. Our recommendations regarding the note issue have accordingly been framed with the express purpose of justifying the confidence of the Indian public in the note by the provision of an adequate metallic reserve and the grant of ample facilities for converting the note into coin. We also take into account the necessity of avoiding on the one hand the inconveniences attending an inelastic currency, and on the other the risks of inflation arising from a currency which can be expanded with undue ease.

76. At the outbreak of war the limit to the invested portion of the Paper Currency Reserve was 14 crores, of which 4 crores might be held in sterling securities, defined as " Securities of the United Kingdom of Great Britain and Ireland or securities issued by the Secretary of State for India in Council under the authority of Act of Parliament, and charged on the revenues of India." The great expansion of the note-issue during the war, coupled with the difficulty of obtaining gold or silver, made it necessary to enlarge these limits. The limits of investment were modified by no less than nine Acts and Ordinances, and the statutory maximum is now 120 crores, of which 20 crores may be held in securities of the Government of India. The increased powers of investment taken since the outbreak of the war are temporary and will, unless re-enacted, lapse six months after the official date for the termination of the war.

77. The Chamberlain Commission commented in paragraphs 103 to 105 of their Report on the inelasticity of the Indian paper currency system. The maximum limit for the invested portion of the reserve is fixed by Statute, and when that limit is reached any further increase in the note-issue requires the deposit of an exactly equal amount of gold or silver in the reserve. Special application to the legislature is necessary when an increase in the circulation renders it expedient to increase the amount of the invested reserve. It may be added that legislation would equally be required if a decrease in the circulation made it desirable to reduce the limit of investment. We recognise the special need for caution in dealing with the note-issue in such a country as India, where a large part

of the population is illiterate and the extended use of paper currency is a habit of very recent growth; but we think it essential to introduce some elasticity into the system, and at the same time to obviate the necessity for constant fresh applications to the legislature as the circulation grows. Both these objects can be attained, if instead of laying down that the invested portion of the reserve must not exceed a fixed maximum, the legislature prescribes that it shall not exceed a maximum percentage of the total issue; or, alternatively, that the metallic portion shall not fall below a minimum percentage of the total issue. In recommending that this method should be adopted we find ourselves in accord in principle with the views of the Chamberlain Commission, and also with those expressed in the memorandum[1] annexed to the statement submitted on behalf of the Government of India.

78. Minimum for metallic portion of reserve to be 40 per cent. of gross circulation.—The Chamberlain Commission recommended that the fiduciary portion of the Paper Currency Reserve, which at the time of their Report stood at 14 crores, should be increased at once to 20 crores and should thereafter be fixed at a maximum of the amount of notes held by Government in the Reserve Treasuries, *plus* one-third of the net circulation. The large increase in the note circulation that has taken place during the course of the war and subsequently has modified the position as it existed when the Commission reported. Under their recommendation it would be necessary that on the present basis of circulation the metallic reserve should amount to 119 crores of rupees, as compared with 80 crores so held at the present time. We do not consider that so large a reserve is required for ensuring the convertibility of the note-issue, especially when it is remembered that in the case of any drain arising from demands for foreign remittance the Gold Standard Reserve is also available. We recommend that the statutory minimum for the metallic portion of the reserve should be 40 per cent. of the gross circulation.

It would, of course, be desirable to maintain in the metallic reserve a substantial margin above the statutory minimum, especially at the beginning of the busy season, which always brings a demand for issues of coin.

It might appear that our recommendation is less cautious than that put forward by Mr. Howard,[2] who proposes for the metallic reserve a minimum proportion of 50 per cent. But he applies the percentage not to the circulation of the moment, but to the average of the gross circulation on the closing days of the three preceding financial years. In times when the circulation is growing rapidly the figure so ascertained is greatly reduced. At the present time, for instance, Mr. Howard's proposal would fix the minimum metallic reserve at 56½ crores, while our recommendation would make it nearly 72 crores.

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[1] *See* memorandum by Mr. Howard, Secretary to the Government of India, Finance Department, Appendices, p. 29.

[2] *See* Appendices, p. 33.

79. Composition of fiduciary portion of reserve.—As regards the composition of the fiduciary position of the reserve, we recommend that the amount to be held in securities issued by the Government of India should be limited to 20 crores, the figure at present permissible under the temporary legislation now in force, and that the balance should be held in securities of other Governments comprised within the British Empire. Of the amount so held not more than 10 crores should be invested in securities with more than one year's maturity, and any securities so held should be redeemable at a fixed date. The balance of the invested portion of the reserve over and above the 30 crores already provided for should be held in short-dated securities with not more than one year's maturity, issued by Governments within the British Empire other than the Government of India. The operation of our recommendations may be illustrated by the following figures exhibiting the composition of the reserve as it stood on 30th November 1919, as it would stand if the invested portion stood at the maximum permitted under the existing law and consequently if the metallic reserve was at the minimum permissible, and as it would stand if the metallic reserve did not exceed the minimum permitted under our recommendations:—

—	Gross Note Circulation.	Composition of Reserve (Lakhs of Rupees).				Percentage of Total Metallic Reserve to Gross Note Circulation.
		Silver.	Gold.	Securities (Indian).	Securities (British).	
Actual figures for 30th November 1919.	179,67	47,44	32,70	17,03	82,50	44·6
Figures showing maximum fiduciary issue under present law.	179,67	59,67		20,00	100,00	33·2
Figures showing maximum fiduciary issue under proposals in report.	179,67	71,87		20,00	87,80*	40

* Securities issued by Governments within the British Empire.

These are our proposals regarding the permanent constitution of the Paper Currency Reserve, but we recognise that it may not be possible to maintain continuously such a large proportion of the reserve in metal in the immediate future. We accordingly recommend that, when permanent legislation is introduced in replacement of the present temporary provisions, authority for retaining for a limited period the existing permissive maximum of 120 crores for the fiduciary issue should be sought.

Revaluation of sterling investments and gold in reserve.—The change in the gold equivalent of the rupee will in-

volve a revaluation of the sterling investments and gold now held in the reserve. We recommend that the sterling investments should be valued at the rate of 10 rupees to the £, no account being taken for this purpose of the temporary depreciation of sterling in terms of gold. The revaluation of the sterling investments and gold at 2*s.* to the rupee will lead to a deficiency amounting to Rs. 38·4 crores in the reserve. It will be impracticable to make good this deficiency at once, but we are of opinion that any savings or profits arising from the rise in the equivalent of the rupee from 1*s.* 4*d.* to 2*s.* gold, such as the saving in the remittances made to meet the direct Home expenditure of the Government of India, will supply a suitable means for discharging this liability in a limited number of years.

80. Limited powers of expansion in view of seasonal demand for currency.—While our recommendations introduce a measure of elasticity into the Indian note-issue, we think it desirable to provide for a further limited power of expansion with a special view to meeting the seasonal demand for additional currency which is normal in India. The proposals formulated by Mr. Howard contemplate that the note-issue should be based in part upon commercial bills of exchange. We have given careful consideration to this plan, with special reference to its application on the largest scale as the basis of the Federal Reserve Note system in the United States of America; and we recommend that it should be tried experimentally in India on a small scale, as the basis for the special power of expansion which we find to be advisable. The requirements of the case would, we think, be met by authorising in the first instance the issue of notes up to 5 crores on the security of commercial bills of exchange in addition to the normal issue. The issue would take the form of loans to the Presidency Banks on the collateral security of bills endorsed by the Presidency Banks and having a maturity not exceeding 90 days. The interest charged to the banks for such advances should be not less than 8 per cent. per annum. The advances should be outside any loans made from Government Treasury balances. The bills tendered as collateral should be *bonâ fide* commercial bills against goods under export, not only because such bills would lead to the automatic retirement of the emergency note-issue on their maturity, but also because such bills are more easily identifiable as representing a definite commercial transaction than internal bills which may be created for purposes of finance or against goods held for speculative transactions. If the difficulty of connecting internal bills with definite transactions in commodities can be overcome, we should see no objection hereafter to authorising the tender of such bills as collateral in addition to export bills, but we think that at the inception of a scheme which is admittedly experimental it would be wiser to authorise the tender of export bills only.

81. Location of Paper Currency Reserve.—The location of the Paper Currency Reserve has given rise to considerable discussion in the past. The main facts of the position may be stated

as follows:—The reserve exists primarily for the redemption of notes, and the proper place for holding the greater part of the reserve must therefore be in India where the notes may have to be met. The silver reserves should, therefore, as in the past, be normally held in India, but silver under purchase or in the course of shipment should be treated as part of the reserve pending its arrival in India.

Gold in Paper Currency Reserve.—The gold also in the Paper Currency Reserve should normally be held in India; but some Paper Currency Gold may at times be held in London, either because it has been purchased there and is awaiting shipment, or because it is held in anticipation of its use in payment for purchases of silver.

Of the securities held in the Paper Currency Reserve, the Government of India's securities would naturally be held in India, while the remainder would be held in the United Kingdom where they would be redeemable or realisable in event of need.

82. Facilities for encashment of notes.—As soon as circumstances permit, free facilities for the encashment of notes should be given, and the restrictions imposed during the course of the war should be withdrawn. We do not suggest that the legal obligation of Government to encash notes should be extended beyond the Currency Offices, but we are satisfied that the additional facilities provided by the Government have tended to encourage confidence in the note-issue, and we would, therefore, welcome their restoration, although we recognise that this may not be practicable at the moment. The obligation of the Government to redeem its notes should be to redeem them in full legal tender coin. It is not necessary that the public should have the option of demanding gold or silver when they present notes. The choice of the metal should be, as it is now, at the option of the Government, who would, no doubt, in normal conditions endeavour to make payment in whatever form of currency is preferred by the tenderer of the note.

Gold Standard Reserve.

83. Amount of reserve.—The Chamberlain Commission held that no limit could be fixed at the time when they reported to the amount up to which the Gold Standard Reserve should be accumulated, and that the profits on the coinage of rupees should continue to be credited exclusively to the reserve. During the war the circumstances have been abnormal, and we consider that it will be advisable to await the return of normal conditions before fixing any maximum figure for the reserve. In reaching this conclusion we are also influenced by the proposal we have made in regard to the new ratio for the rupee. So long as prices throughout the world remain at or about the present level, we believe that India will maintain a prosperous export trade, and that the present strength of the Gold Standard Reserve, assisted by the other resources at the disposal of the Secretary of State, will suffice to maintain the ex-

change value of the rupee at the point we suggest. But if there were a sudden fall in world prices it is possible, as we have pointed out in paragraph 51, that the normal current of Indian trade might be affected for a period, and that a heavier call might be made on the resources for supporting exchange than has occurred in the past. We hold, therefore, that when profits again accrue on the coinage of rupees they should be credited in their entirety to the reserve.

84. Composition of reserve.—The recommendation of the Chamberlain Commission that the silver branch of the Gold Standard Reserve, which in June 1914 amounted to 6 crores of rupees, should be abolished, has already been carried out.

At present the reserve is held almost entirely in securities, and on the 30th November 1919 was constituted as follows, the figure given representing in each case the face value of the security:—

	£
British Treasury Bills, maturing between December 1919 and March 1920	8,219,000
Exchequer Bonds, redeemable between February 1920 and October 1921	16,199,300
National War Bonds, redeemable 1st October 1922	7,500,000
Five per cent. War Loan, 1929-47	3,762,181
Local Loans, 3 per cent. Stock	200,000
Irish Land Stock, 2¾ per cent.	438,720
Transvaal Government 3 per cent. Guaranteed Stock, 1923-53	1,092,023
	37,411,224
Cash	27,093
TOTAL	37,438,317

The Chamberlain Commission were of opinion that a considerable portion of the reserve should be held in gold, and suggested that the total gold holding should be raised as opportunity offered to 15,000,000*l.*, and that the authorities should thereafter aim at keeping one-half of the total reserve in actual gold. We agree in principle that the reserve should contain a considerable proportion of gold, but we do not anticipate that under the changed conditions a large gold holding will be attainable for some years, and we feel that in the present state of the note-issue such gold as the Government of India can obtain should be added to the Paper Currency Reserve rather than to the Gold Standard Reserve. At the present moment, therefore, the most satisfactory course lies in keeping the reserve as liquid as possible by an ample holding of securities with early dates of maturity. This condition is secured under the present scheme of investment. From the statement given above it will be seen that, with the exception of about 5,500,000*l.*, the securities in the reserve are redeemable by October 1922 at the latest. We are of opinion that the amount of securities with a maturity exceeding three years should not be increased, and that the authorities

should aim at holding all the invested portion of the reserve in securities issued by Governments within the British Empire (other than the Government of India), and having a fixed date of maturity of not more than 12 months.

85. Location of the Gold Standard Reserve.—The object for which the Gold Standard Reserve exists is to afford protection against a fall in exchange by meeting demands for sterling remittance to London; and it is evident that its resources will be most readily available for this purpose if they are held in London. This consideration has governed the location of the fund hitherto, and was considered by the Chamberlain Commission to be decisive.

There is, however, a strong sentiment in India in favour of the location of the whole, or at any rate a large part, of the reserve in India. In currency matters the possession of public confidence is an asset of great value, and we therefore think it advisable to comply with the Indian demand, so far as this can be done without detracting from the utility of the fund for the purposes for which it exists. Gold in India can be made available for the purpose of foreign remittance, either by export or by transfer to the Paper Currency Reserve in India against a corresponding release of Paper Currency assets in the United Kingdom or, in circumstances of urgency, by arranging to earmark it for the Bank of England. We consider, therefore, that a portion of the gold in the Gold Standard Reserve should be held in India; but the gold so held should not exceed one-half of the total, and steps should be taken to ensure that it is not made available to the public except for the purpose of export.

The sterling investments of the Gold Standard Reserve (including cash on deposit) should, as in the past, continue to be held in London.

86. Minority Report by Mr. Dalal.—Our colleague, Mr. Dalal, submits a separate report. While we regret that he does not share our conclusions, we wish to record our appreciation of the assistance which we have derived from his knowledge and experience.

Summary of Conclusions.

87. Summary of conclusions.—We now proceed to summarise the main conclusions at which we have arrived.

(*i*) It is desirable to restore stability to the rupee and to re-establish the automatic working of the Indian currency system. (Para. 36.)

(*ii*) The reduction of the fineness or weight of the rupee (para. 38), the issue of 2- or 3-rupee coins of lower proportional silver content than the present rupee (para. 39), or the issue of a nickel rupee (para. 40), are expedients that cannot be recommended.

If the legal tender limit of one rupee for the 8-anna nickel coin should prove an obstacle to its free circulation the question of raising the limit to Rs. 5 or Rs. 10 should be considered. (Para. 40.)

(*iii*) The maintenance of the convertibility of the note-issue is essential, and proposals that do not adequately protect the Indian paper currency from the risk of becoming inconvertible cannot be entertained. (Para. 41.)

(*iv*) The rise in exchange, in so far as it has checked and mitigated the rise in Indian prices, has been to the advantage of the country as a whole, and it is desirable to secure the continuance of this benefit. (Para. 50.)

(*v*) Indian trade is not likely to suffer any permanent injury from the fixing of exchange at a high level.

If, contrary to expectation, a great and rapid fall in world prices were to take place, and if the costs of production in India fail to adjust themselves with equal rapidity to the lower level of prices, then it might be necessary to consider the problem afresh. (Para. 51.)

(*vi*) The development of Indian industry would not be seriously hampered by a high rate of exchange. (Para. 52.)

(*vii*) The gain to India of a high rate of exchange for meeting the Home charges is an incidental advantage that must be taken into consideration. (Para. 53.)

(*viii*) To postpone fixing a stable rate of exchange would be open to serious criticism and entail prolongation of Government control. (Para. 58.)

(*ix*) The balance of advantage is decidedly on the side of fixing the exchange value of the rupee in terms of gold rather than in terms of sterling. (Paras. 56-7.)

(*x*) The stable relation to be established between the rupee and gold should be at the rate of Rs. 10 to one sovereign, or, in other words, at the rate of one rupee for 11·30016 grains of fine gold, both for foreign exchange and for internal circulation. (Para. 59.)

(*xi*) If silver rises for more than a brief period above the parity of 2*s*. (gold), the situation should be met by all other available means rather than by impairing the convertibility of the note-issue. Such measures might be (*a*) reduction of sale of Council bills; (*b*) abstention from purchase of silver; (*c*) use of gold to meet demands for metallic currency. If it should be absolutely necessary to purchase silver, the Government should be prepared to purchase even at a price such that rupees would be coined at a loss. (Para. 59.)

(*xii*) Council Drafts are primarily sold not for the convenience of trade but to provide for the Home charges in the widest sense of the term. There is no obligation to sell drafts to meet all trade demands; but, if without inconvenience or with advantage the Secretary of State is in a position to sell drafts in excess of his immediate needs, when a trade demand for them exists, there is no objection to his doing so, subject to due regard being paid to the principles governing the location of the reserves.

Council Drafts should be sold as now by open tender at competitive rates, a minimum rate being fixed from time to time on the basis of the sterling cost of shipping gold to India. At present this rate will vary; but when sterling is again equivalent to gold, it will remain uniform. (Para. 61.)

(*xiii*) The Government of India should be authorised to announce, without previous reference to the Secretary of State on each occasion, their readiness to sell weekly a stated amount of Reverse Councils (including telegraphic transfers) during periods of exchange weakness at a price based on the cost of shipping gold from India to the United Kingdom. (Para. 62.)

(*xiv*) The quantity of gold taken by India for all purposes in the period before the war was not disproportionately large having regard to her social customs and economic position; but more produtive methods for employing wealth should be encouraged. (Paras. 63-4.)

(*xv*) The import and export of gold to and from India should be free from Government control. (Para. 65.)

(*xvi*) The Government should continue to aim at giving the people the form of currency which they demand, whether rupees, notes, or gold; but gold can be employed to the best advantage in the Government reserves, where it is available for meeting the demand for foreign remittance.

It would not be to India's advantage actively to encourage the increased use of gold in the internal circulation, but it may for some time be difficult to meet all demands for metallic currency in rupees, and a more extensive use of gold may be necessary. In order that confidence may not be disturbed by exceptional issues, the issue of gold coin in moderate quantities should be one of the normal methods of meeting demands for currency. (Para. 66.)

(*xvii*) The Bombay branch of the Royal Mint should be re-opened for the coinage of sovereigns and half sovereigns and facilities should be afforded to the public for the coinage of gold bullion and for the refining of gold. (Para. 67.)

(*xviii*) The obligation of the Government to give rupees for sovereigns should be withdrawn. (Para. 68.)

(*xix*) Opportunities should be afforded to the public to exchange sovereigns in their possession at the rate of 15 rupees per sovereign at the time of the introduction of the new ratio. Similar opportunities should be given to holders of the gold mohur which should eventually be demonetised. (Para. 69.)

(*xx*) The prohibition on the import of silver should be removed as soon as is convenient. (Para. 70.)

(*xxi*) When the prohibition on the import of silver is removed, the import duty should also be removed, unless the fiscal position demands its retention. (Para. 71.)

(*xxii*) The prohibition on the export of silver should be retained for the present with a view to the protection of the silver currency from depletion by export.

If the silver mined in India should cease to be purchased by the Government, its export should be permitted under licence. (Para. 72.)

(*xxiii*) Improved banking facilities and increased opportunities for the investment of savings should be afforded. (Para. 73.)

(*xxiv*) No recommendation is made for modifying the present practice regulating the purchase of silver for coinage. (Para. 74.)

(*xxv*) The statutory minimum for the metallic portion of the Paper Currency Reserve should be 40 per cent. of the gross circulation.

As regards the fiduciary portion of the reserve, the holding of securities issued by the Government of India should be limited to 20 crores. The balance should be held in securities of other Governments comprised within the British Empire, and of the amount so held not more than 10 crores should have more than one year's maturity, and all should be redeemable at a fixed date. The balance of the invested portion above these 30 crores should be held in short-dated securities, with not more than one year's maturity, issued by Governments within the British Empire.

The existing permissive maximum of 120 crores should be retained for a limited period.

The sterling investments and gold in the Paper Currency Reserve should be revalued at 2*s*. to the rupee. The depreciation which will result from this revaluation cannot be made good at once, but any savings resulting from the rise in exchange will afford a suitable means for discharging this liability in a limited number of years. (Paras. 78, 79.)

(*xxvi*) With a view to meeting the seasonal demand for additional currency, provision should be made for the issue of notes up to five crores over and above the normal fiduciary issue as loans to the Presidency Banks on the security of export bills of exchange. (Para. 80.)

(*xxvii*) The silver and gold in the Paper Currency Reserve should be held in India except for transitory purposes. (Para. 81.)

(*xxviii*) As soon as circumstances permit, free facilities for the encashment of notes should be given, and the restrictions imposed during the war should be withdrawn. The Government should have the option of redeeming its notes in full legal tender gold or silver coin. (Para. 82.)

(*xxix*) No limit can yet be fixed to the amount up to which the Gold Standard Reserve should be accumulated and when profits again accrue on the coinage of rupees they should be credited in their entirety to the reserve. (Para. 83.)

(*xxx*) Under present conditions Government should hold such gold as they obtain in the Paper Currency Reserve rather than in the Gold Standard Reserve. The Gold Standard Reserve should when practicable contain a considerable proportion of gold; but the most satisfactory course at present lies in keeping the reserve as liquid as possible by the holding of securities with early dates of maturity.

The amount of securities in the reserve with a maturity exceeding three years should not be increased, and the aim should be to hold all the invested portion of the reserve in securities issued by Governments within the British Empire (other than the Government of India) and having a fixed date of maturity of not more than 12 months. (Para. 84.)

(*xxxi*) A portion of the gold in the Gold Standard Reserve, not exceeding one-half, should be held in India; the sterling investments should continue to be held in London. (Para. 85.)

88. We desire to place on record our high appreciation of the services rendered by Mr. C. H. Kisch, C.B., and Mr. H. Denning, I.C.S., as Secretaries to the Committee. They have discharged the duties entrusted to them with unfailing promptness and courtesy, and their valuable assistance has greatly facilitated our enquiry.

(Signed) H. BABINGTON SMITH.

CHALMERS.

MARSHALL REID.

J. B. BRUNYATE.

F. C. GOODENOUGH.

C. S. ADDIS.

C. T. NEEDHAM.

M. M. S. GUBBAY.

W. B. HUNTER.

T. W. McMORRAN.

C. H. Kisch,

H. Denning,

Secretaries.

Dated the 22nd day of December 1919.

MINORITY REPORT BY MR. DADIBA MERWANJEE DALAL.

TO THE RIGHT HON. EDWIN S. MONTAGU, M.P., SECRETARY OF STATE FOR INDIA.

INTRODUCTORY, WITH RECOMMENDATIONS.

1. I regret that the divergence of opinion between my colleagues on the Committee and myself on vital currency principles is so great as to render it impossible for me to concur with the views of the majority.

2. The tragedy of the great war in its world-wide effects has dealt very unequally with different countries. To India as a whole it brought a period of great economic prosperity, because India was able to supply produce and material which were urgently required in connection with the prosecution of the war, besides taking a full active part in the conflict. Notwithstanding this prosperity, which might have been expected to increase her financial strength, India has been called upon to face a veritable revolution in her currency arrangements which must cause widespread and lasting hardship amongst the masses of the people of India.

3. This revolution has been brought about by the executive action of the authorities by means of raising the sterling rate of exchange. The only occasion on which this Committee were consulted regarding the changes made was when the rate was altered from 2*s.* to 2*s.* 2*d.* Against this alteration I felt it to be my duty to protest.

4. The rate of exchange was raised by stages from the normal rate of 1*s.* 4*d.* to 2*s.* 4*d.*, and the reason assigned was that, owing to the rise in the price of silver, the bullion value of the rupee was above the rate fixed from time to time in relation to sterling. But that reason cannot be held to be the sole reason, since even if the price of silver should fall the intention is to maintain the rate of exchange at a much higher level than 1*s.* 4*d.*

5. I cannot acquiesce in the great change in the money arrangements of India which must accompany this alteration in the rate of exchange. The legally established money standard is the sovereign, with rupees definitely related thereto at the rate of 15 to 1. That standard ratio has been broken by the raising of the rate of exchange, and I hold that it is vitally important that that ratio should be maintained.

6. In my opinion the reason given for raising the rate of exchange is altogether inadequate. The rise in the price of silver could have been prevented by removing the embargo on exports of silver from India after the war had ended, and it was after the war that the greater part of the rise in exchange was brought into force. India could easily have spared silver for export; such exports would

have been profitable to her, and they would have prevented the great rise in the price of silver upon which so much has been made to depend through the raising of the rate of exchange. It was chiefly because the export of silver from India was prohibited, and because India was made a potential buyer instead of a seller, that the silver markets were inflamed and the price was raised.

7. Even if silver exports from India were not considered desirable there was still no occasion for raising the rate of exchange after the war because of the rise in the price of silver. It would only have been necessary to stop the sale of rupee bills by Government in excess of their own Treasury requirements and leave the balance of trade to be adjusted by other means than silver.

8. There was one important obstacle to the removal of the embargo on silver exports. The paper currency had been heavily watered by the issue of notes not backed by coin but by British Treasury bills held in London. As a war measure and a temporary expedient to meet the difficulties of the time this might have been excused. After the war, however, this temporary expedient had the effect of blocking the removal of the embargo on silver exports by providing the only strong reason for retaining it, namely, the protection of the paper currency coin reserves against withdrawals of silver for export. This temporary expedient, therefore, turned to the permanent disadvantage of India when it provided a reason for retaining the embargo. But the necessity for protecting in this way the paper currency coin reserves was due to the very artificial conditions created by the extensive watering of the note-issue, and consequently the need for the embargo was artificial.

9. As long as a world-wide embargo on gold exports existed a rise to some extent in the rate of exchange could not, perhaps, be temporarily avoided; but when the United States became a free market for gold on the 9th June, 1919, and the gold production of South Africa became available to the highest bidders in London from the 18th July, 1919, the need for further raising the exchange rate from 1*s*. 8*d*. by four stages to 2*s*. 4*d*. was absolutely uncalled for.

10. These new currency arrangements must, if continued, have disastrous consequences to India and to the people of India. They must seriously disturb the relations existing between creditor and debtor. They will cause dislocation and a set-back to several Indian industries and vast continuous losses on the exports of Indian produce. There is a danger of India's balance of trade turning against her and so checking her prosperity. And it should be remembered that between 100 and 200 millions of people live on the brink of starvation, and a great permanent change in the rate of exchange must ultimately bring intense distress to millions of the helpless masses. A fixed high level of exchange must also cause enormous losses in the rupee value of the invested reserves in sterling securities and of gold held as part of the metallic reserves against the note issue. It will also cause a colossal loss if the sovereigns now

held by the Indian public, estimated to amount to about 50,000,000, have to be redeemed at the statutory rate of 15 rupees to the sovereign.

11. In my opinion the gold exchange standard as applied to India is entirely discredited as a currency system intended to meet Indian conditions. I make every allowance for the difficulties with which it had to contend during and since the war, but the raising of the rate of exchange after the war was over was wholly unnecessary. The people of India have strong objections to the purchase of silver at the present inflated and thoroughly artificial price.

12. I discuss in detail below these and other points referred to the Committee, and now state here the recommendations I desire to make:—

(*a*) The money standard in India should remain unaltered; that is, the standard of the sovereign and gold mohurs with rupees related thereto at the ratio of 15 to 1.

(*b*) Free and unfettered imports and exports by the public of gold bullion and gold coins.

(*c*) Free and unfettered imports and exports by the public of silver bullion and silver coins.

(*d*) The gold mint at Bombay to be continued and to receive gold bullion from the public and to coin free of charge gold mohurs of the same exact weight and fineness as the sovereign and to hand them over to the tenderers of gold bullion in less than 15 days.

(*e*) The Bombay mint to undertake refining of raw gold for the public and not to make any profit on the transaction.

(*f*) The existing silver rupees of 165 grains of fine silver at present in circulation to continue full legal tender.

(*g*) As long as the price of silver in New York is over 92 cents Government should not manufacture silver rupees containing 165 grains fine silver.

(*h*) As long as the price of silver is over 92 cents Government should coin 2-rupee silver coins of reduced fineness compared with that of the present silver rupee and the same to be unlimited legal tender.

(*i*) Government to coin a new 8-anna silver piece of reduced fineness and the same to be unlimited legal tender.

(*j*) Government not to coin an 8-anna nickel piece.

(*k*) Government to sell Council bills by competitive tenders for the amount defined in the Budget as required to be remitted to the Secretary of State. The Budget estimate to show under separate headings the amount of Council bills drawn for Home Charges, for Capital Outlay and Discharge of Debt. Council bills to be sold for Government requirements only and not for trade purposes,

except for the purpose mentioned in the next succeeding recommendation.

(*l*) "Reverse" drafts on London to be sold only at 1*s.* $3\frac{29}{32}$*d.* The proceeds of "Reverse" drafts to be kept apart from all other Government funds and not to be utilised for any purpose except to meet drafts drawn by the Secretary of State at a rate not below 1*s.* $4\frac{3}{32}$*d.* per rupee.

(*m*) Currency notes should be printed in India.

(*n*) Government not to interfere with the immemorial practice of the Indian public of melting current coins.

(*o*) The sterling investments held against the Indian note issue to be liquidated as early as possible and transmitted to India in gold.

(*p*) The use of one rupee currency notes to be discontinued as early as possible and meanwhile not to be forced into circulation.

Report on the Terms of Reference.

13. The Terms of Reference to the Committee were as follows:—

"To examine the effect of the war on the Indian exchange and currency system and practice and upon the position of the Indian note issue, and to consider whether in the light of this experience and of possible future variations in the price of silver, modifications of system or practice may be required, to make recommendations as to such modifications, and generally as to the policy that should be pursued with a view to meeting the requirements of trade, to maintain a satisfactory monetary circulation, and to ensuring a stable gold exchange standard."

I.—*Breakdown of the Standard Ratio between Rupees and the Sovereign.*

14. The outstanding effect on the Indian exchange and currency system has been that the system has broken down at a time when India enjoyed a large measure of prosperity as displayed by the foreign trade returns. The undertaking by the authorities to supply rupees without limit of amount at the rate of fifteen to the sovereign could not be maintained owing to the rise in the price of silver which made it impossible to supply fresh rupees (containing 165 grains of fine silver) at that ratio without loss. In consequence of this rise in the price of silver the standard ratio of rupees to the sovereign was given up, the sterling rate of exchange for the rupee was raised by stages to 2*s.* 4*d.*, and the Secretary of State for India is now selling rupee bills at that rate which makes the present relationship of the rupee to the sovereign in working practice 11 to 1.

15. It is true that the main object which the authorities kept before themselves in working the system was to maintain the exchange value of the token rupee in meeting foreign payments. In the words of the Chamberlain Commission the "cardinal feature" of the system was "absolute security for the convertibility into sterling of so much of the internal currency as may at any moment be required for the settlement of India's *external* obligations." But whatever object the authorities had in view in working the system, this cannot alter the fundamental fact that the Indian currency was founded on the sovereign (a full value gold coin) as the money standard with rupees (token silver coins) definitely related to the sovereign at the rate of 15 to 1, and if it is impossible to maintain this ratio between the sovereign and rupees I consider that the system has failed in its most important part.

16. In support of this opinion it is necessary to recall the alterations made in the Indian currency arrangements in 1893. Up to that time India had a silver standard with mints open to the free coinage of silver. The mints were then closed and the silver standard was given up. The silver standard was replaced a few years later by the standard of the sovereign, sovereigns and half-sovereigns being made legal tender for 15 and 7½ rupees respectively, rupees being thus definitely connected with the sovereign at the ratio of 15 to 1 and also remaining full legal tender.

17. There has been a difference of opinion as to the effect of these alterations in the currency arrangements. According to information placed before the Committee they have sometimes been described as having placed India on a gold standard, while, on the other hand, some authorities prefer to describe the Indian standard of value as a gold exchange standard since the effectiveness of the arrangements largely depended in practice on the action of the Secretary of State and the Government of India in selling or exchanging rupees for gold or sterling and sterling for rupees. But whether the standard is called a gold standard or a gold exchange standard, the alterations referred to could have no meaning except on the hypothesis that the money standard had been changed from a silver standard to the standard of the sovereign and that rupees were in effect made a fixed fraction of the sovereign. I cannot conceive that the mere title by which the standard is described, or any mere arrangements followed in working practice, can admit of any alteration of the ratio legally established between the rupee and the sovereign.

18. It seems to me to be impossible to exaggerate the importance of the legal standard for money payments. This standard should be and usually is regarded as less open to repeal or modification than perhaps any other legislative Act. It gives the people rights as to the kind of money they may demand in exchange for their labour or goods, rights which cannot be removed or modified without inflicting widespread injury and risking the gravest discontent. The Indian money standard was definitely changed from silver to

gold so recently as 1893 for reasons affecting directly the Government of India and the Indian people, and proved to be of great benefit to India as a whole. But it is impossible to contemplate another permanent change in the rupee value of the sovereign for reasons which have not originated in India and at a time when neither the Government (apart from the part they play in the currency policy) nor the public have been inconvenienced by the standard legally established.

19. It is true that under the stress of war it has been a common expedient of Governments concerned to treat their money standards as of little account and to resort to inflation of currency as a means of conducting the finance of war. No such reason applies to the Indian case. The inflation of the Indian currency during the war was a genuine inflation as distinguished from the artificial inflation witnessed in most of the belligerent countries. It arose from the balance of indebtedness due to India. The breakdown of the system was not due to war expenditure by the Government of India. It was caused by the acceptance in London of payments due to India in the form of sterling, which could not be transmitted to India by the usual methods. The commitments to India of the belligerent nations, as to other countries, could not be met in the usual manner through exchange operations or specie remittances. They were, in fact, unable to pay in international money, and obviously the best course to follow was that in fact followed in settling similar commitments in the United States by the flotation of loans.

20. Unfortunately, India had not been prepared financially for absorbing her favourable trade balances in any other form than the precious metals. Although India is normally a creditor country with trade balances running highly favourable to her, other means of adjusting favourable balances than the precious metals have not been actively sought for. That is one of the disadvantages of currency arrangements conducted by the Government. Great Britain as a creditor country set an excellent example of cancelling her favourable balances by investments abroad. There has been no encouragement in India of that method of settling trade balances. There is far more British and other money invested in India than Indian money invested abroad. Still, there is little room for doubt that, during the war, British Government loans could have been successfully floated in India on a very large scale, on the same lines and terms as some of those publicly floated in the United States to meet the expenditure of the Imperial Government. It is also probable that something could have been done to encourage Indian investors to buy the Indian sterling loans held in London, if arrangements had been made for payment of the interest at the Government district treasuries in India.

21. The break in the standard ratio during the war was, however, less serious than the still greater break during the present year. The overwhelming demands for war requirements were at an end, and, although trade demands were urgent, it was imperative, in the

interests of the great majority of the people of India, that their rights in the standard money of the country should have been protected from further modification. Trade and circumstances, especially in peace, must conform to the standard of money rather than that the money standard should accommodate itself to them. If it was impossible to meet trade demands without breaking the standard, that would be a reason for declining to meet them, but hardly a reason for meeting them and breaking the standard.

II.—*Watering the Note-Issue.*

22. With regard to the note-issue there has been a complete reversal of the procedure formerly observed in the matter of the fiduciary issue the effect of which on the note-issue itself can only be described as extremely unfortunate. The former practice was to increase the fiduciary issue by investment of a portion of the metallic reserves, and this was done only when the proportion of the latter to the total of the notes in active circulation had shown, over a considerable period, a position sufficiently strong to warrant an extension of the invested reserves and a corresponding diminution of the metal reserves. During the war, however, the fiduciary issue was expanded to an enormous extent without regard for the considerations which formerly decided extensions of that form of issue. It was no longer a case of investing a portion of the metallic reserves held in India against outstanding notes; notes were boldly issued against which no metallic reserves in India had ever existed. Also the proportion of the metallic reserves to the total of the outstanding notes was not allowed to have any weight. It was a case of simply watering the note-issue in its worse form—issuing notes without any metallic backing. In other words, it was a forced loan from the Indian public free of interest. It was an extreme measure to apply to the Indian note-issue even during the war and at a time when there were immense sums held in London belonging to the Indian currency. Indeed, it appears to have been adopted because of the difficulty of transferring the balances held in London to India. But even so, the warnings which had been given at the outbreak of the war, when there was a run on the paper currency offices for the encashment of notes, should have shown the necessity of maintaining the note-issue in a strong position and the undesirability of weakening it by an overissue of notes.

23. No exception can, of course, be taken to the security held against the notes thus issued which consisted of British Treasury bills, but the better course would have been to invite the public to take up the bills or some other form of British securities. The public might not have cared to accept the same rate of interest as the India Office obtained on the investments, but even if it had been necessary to pay a higher rate of interest it would have been better to face this cost rather than imperil the safety of the note-issue.

24. Not unnaturally there was much discussion as to the note-issue becoming an inconvertible issue, and, indeed, an actual state of inconvertibility was only avoided by the narrowest of margins. To my mind inconvertibility would be a disaster of the first magnitude for the note-issue and for India. It would destroy all confidence in Government's own paper money. Not only so but, seeing that British Government securities are so largely held against the note-issue (the amount is Rs. 835,000,000 which, at the present rate of exchange of 2*s.* 4*d.*, is approximately 93,000,000*l.*), the credit of Great Britain is also involved.

25. I have mentioned that an actual state of inconvertibility was avoided only by the narrowest of margins. This was aided by the exceptional measures taken restricting the movement of coin by rail and steamer, which had the effect of confining exchangeability of notes into coin to the seven head currency offices. Even now in these offices conversion of notes into coin is directly and indirectly impeded.

26. Nothing can better show the effect on the public mind of the great expansion in the fiduciary issue and the methods adopted to avoid demands for encashment than the fact that currency notes were quoted at a heavy discount. A telegram from the Viceroy, dated the 8th November, 1919, stated that the highest rates of discount on currency notes reported during 1918 were 19 per cent. in the Central Provinces, 15 per cent. in Bengal, 13½ per cent. in Burma, but his Excellency added that during 1919 the highest rate reported was 3 per cent. This telegram showed not only a very high rate of discount in 1918, but also that it was widely spread throughout the country, and while it is satisfactory that the rate of discount has fallen to a low figure this year, the fact that such a considerable discount existed is one that must have a lasting influence on the minds of the public. The Governor of the Bank of England, in the course of his evidence before the Committee, remarked that a premium on gold was a very vicious thing. I think that, in the sense that a premium on gold is vicious, a discount on currency notes within India is equally vicious.

27. In view of the great disturbance to the credit of the paper currency arising from the great expansion of the fiduciary issue, I consider that the metal reserves should be strengthened as early as possible by the liquidation of the reserves invested in London, and also that, in order to re-establish confidence, a high percentage of cash reserves should be maintained for many years to come. About 80 per cent. would not be too high a figure to fix as a normal proportion of metallic reserves to the total of notes outstanding. It must be remembered that this metallic proportion on the 31st March of each year from 1910 to 1915 inclusive averaged 78·2 per cent.

28. A well-conducted note issue is not only an economical and therefore profitable form of money, but also has an important educative effect in a country like India with a backward and ignorant

mass of people. Also, it should be remembered that the internal trade of India is much larger than the external trade. Mr. E. M. Cook, C.I.E., of the Finance Department, has expressed the opinion that the internal trade is certainly fifteen times larger than the external trade, and that possibly the proportion is even higher. The ultimate possibilities of extending the note-issue are therefore very great, but the first essential is to ensure that there shall be no grounds for distrust of the issue, and particularly that nothing should be done to give cause for the notes to pass at a discount.

III.—*The Price of Silver.*

29. The Committee were also asked to consider the bearing of possible future variations in the price of silver on the currency system and practice. The reference of this question to the Committee shows the great importance attached by the authorities to the continued use of silver in settling India's trade balances, even although the use of silver cannot be continued for the present without breaking the standard ratio. It is, in fact, the crux of the whole situation.

30. Information placed before the Committee lays great stress on the effect of the Pittman Act in the United States in its reaction on the price of silver and on the Indian currency position, and it was the high price of silver which was the reason given for raising the rate of exchange during recent months which had the effect of altering the standard ratio between rupees and the sovereign.

31. It is almost impossible to exaggerate the effect on the silver market of the raising of the rate of exchange for the rupee and making the rate more or less closely dependent on the price of silver on the ground that that price made the rupee more valuable as bullion than as a coin if the rate was not altered. It excited and inflamed the silver markets with anticipations of continued buying on account of the Indian currency at rising prices, and there are not wanting signs that silver interests are prepared to take full advantage of the situation created by this measure.

32. I am unable to fall in with the idea that the rise in the price of silver afforded solid ground for this recent great alteration in India's money standard. On the contrary, I contend that the price of silver has been artificially forced to its high level by the exclusion of stocks of Indian silver from the world's markets by means of the continuance of the prohibition of exports of silver, and the raising of the exchange rate. The position is that the American production of silver is shut out of the world's market automatically by the operation of the Pittman Act if the price of silver should fall below 1 dollar per fine ounce. The Act requires that until the silver taken from the dollar reserves is restored, the United States Treasury must buy at 1 dollar per fine ounce any silver of American origin tendered to it at that rate. This provision in the Pittman Act has been taken as establishing in effect 1 dollar per fine ounce as the minimum price of silver until the

amount of silver withdrawn from the dollar balances has been restored, and since the silver dollars withdrawn under the Pittman Act for the Orient represent between twice and three times the normal American production, it is estimated that the process of restoration will extend over a period of several years. The future production of American silver being thus assured of a market at a stated price, owing principally to the demands for Indian coinage during the war, and the current of trade showing the probability of fresh demands for India, while China was a keen buyer, it was only to be expected that the price of silver would rise. At the moment of writing the price in London is about 78*d.* This price has been made possible only by the prohibition of exports of silver from India and by the raising of the rate of exchange, which has the effect of lowering the rupee value of all silver held there and making exports unprofitable. But for the prohibitory orders and the raising of the rate of exchange it would have been profitable for Indian holders to sell silver, and Indian sales would have prevented the great rise in price which has taken place. Under these circumstances, the high world price of silver can only be regarded as wholly artificial, and consequently as a reason for such a drastic step as the alteration of the money standard ratio between rupees and the sovereign has no weight.

33. It is frequently said that India is a sink for the precious metals and never allows them to come out. Here was an opportunity of disproving such statements. Silver would have been freely exported but for the measures taken by Government to prevent exports.

34. The exclusion of India's silver from the world's market is not altogether a new thing. It was practically excluded by imposing a duty on silver imports and not refunding the full duty paid when the silver was re-exported, and granting no refund of duty whatsoever on melted silver ornaments coming from the districts even in time of famine. I add a note on this subject in the ancillary problems dealt with at the end of this report.

35. There is the objection that it was necessary to protect the silver currency against depletion by export by means of ordinances forbidding exports. This is an objection which would have very great force in a country like the United Kingdom where the subordinate silver currency forms a small percentage of the total amount of all kinds of currency in active circulation the loss of which by export would cause the greatest inconvenience. In India it has very little force because the total amount of silver currency is far in excess of the quantity in active circulation and held against the note issue. It is estimated that there are about 3,000,000,000 to 4,000,000,000 of rupees in India. Moreover the amount that India could sell for export could not have reached very important dimensions because foreign buying power is limited, while Indian silver

would not be accepted by the United States Treasury to replace the dollar balances since the replacement has to be made from silver of American origin.

36. A more serious objection to permitting silver exports was the extreme vulnerability of the paper currency reserves of coin, because of the extent to which the note issue had been watered by ordinances sanctioning the issue of notes in India against British Treasury Bills held in London. But here again the position was most artificial. The expansion of the note-issue on the security of British Treasury Bills was in effect a forced loan from the Indian people, a method of meeting the difficulties of the time which I venture to suggest should not have been resorted to. The proper course was to suggest to the British Treasury the desirability of floating public loans in India on the lines of those raised by the British Government in the United States, if the payments to India in London could not be completed by transmission to India in the usual manner.

37. A real practical difficulty in the way of removing the embargo on silver exports, as contrasted with the difficulty artificially created by the watering of the paper currency, was that silver exports would have increased the amount of the balance due to India, which the authorities were already unable to transmit to India, and would also have involved a change in the method of adjusting the balances. Obviously, with silver exports, it would have been absurd to continue to settle the trade balances by means of the sale of rupee bills in London. The settlement would have had to be made in gold or by some form of deferred payments. The latter form of adjustment would not have been easy in the absence of preparation of the Indian market to take outside securities. And there would no doubt have been the usual objections to India being paid in gold. Still, I venture to think that even if gold had been required India could reasonably have expected consideration in the special circumstances of the case, especially after the war was over, and the embargo on gold exports had been removed in the principal money centres. The point at issue was a vital one for India, namely, whether India should be compelled to give up a vital part of her established money standard because the price of silver had made her token silver currency more valuable as metal than as coin. India had the power, and it would have been profitable for her and to her interest to prevent the rise in the price of silver by sales of the metal. The mere fact of Indian sales would have broken the strength of the silver market. In such circumstances it would not have been unreasonable for India to ask that her trade balances should be paid in gold so that she should be able to export silver for the preservation of her money standard.

38. Since the above was written it has been reported that the United States Government have followed the method here suggested by offering to sell silver currency when the price of silver went

above the melting value of their silver coinage. It seems to me that what is being done in America could have been done in India.

39. But even if exports of silver were not allowed for the purpose of preventing the price of silver from rising, there was still no occasion to adopt the extreme measure of raising the rate of exchange, and so breaking the standard ratio. India did not require additional supplies of rupees. She could carry on for many years without any new silver coinage. The only alteration required would have been to stop the coinage of rupees, and that would have occurred automatically by reason of the loss coinage would involve. But if the coinage of silver ceased because it was unprofitable, the trade balances if they continued to be favourable would have to be settled by other means than importing silver. It appears to me that the authorities were not willing to permit of a settlement by other means. They had come to regard the practice of selling rupee bills in London without limit of amount as an all essential part of their duties in the administration of the currency which could not be given up. Yet the position proved that there was in fact a limit to the issue of rupees if the standard ratio was to be maintained, since rupees could no longer be coined without loss at that ratio. Rather than give up the sale of rupee bills the authorities raised the rate of exchange, so breaking the ratio, and continued to offer rupee bills for sale.

40. Still another method of avoiding the raising of the rate of exchange because of the high price of silver would have been to impose a duty on all exports at a rate sufficiently high to provide the means of meeting the additional cost of silver over the price at which silver could be bought and coined without loss at the fixed ratio. Such a duty would have the effect of moderating the foreign demand for Indian produce, and thereby moderating the balance of trade due to India; while, on the other hand, if India is compelled to accept payment in silver, the duty would enable India to avoid paying more for it than the price at which it could be bought and coined without loss.

41. The authorities considered that there were only two alternatives open to them, either to raise the rate of exchange or to debase the silver coinage. I have endeavoured to show that there were other courses open to them without raising the exchange or debasing the rupee coins. But even if it were the case that they had only these two alternatives it is by no means certain that they took the better of the two. My own belief is that the people of India would prefer debased silver coins to an alteration of the ratio which the raising of the exchange involves. It would not be practicable or advisable to call in all the rupees in the hands of the public to be recoined, but any new coinage that became necessary could be issued in the form of a special silver coin, such as, for example, a two-rupee coin containing a reduced quantity of silver.

42. In connection with the question of debased coins I may say here, by way of parenthesis, that although the Government of India

have taken power to issue a nickel half-rupee or eight-anna coin I trust that they will hesitate before putting it into circulation, and also that the suggestion which has been made that the eight-anna nickel piece should be made legal tender for a larger amount than one rupee will not be agreed to. The appearance in the currency system of one rupee paper notes and of two-anna nickel coins has sufficiently alarmed the Indian people and led to the hoarding of rupees. It is unsafe to carry the debasement of the coinage any further by the use of nickel coins. I am of opinion that the eight-anna nickel piece should not be put into circulation at all, and I suggest that instead of it an eight-anna silver piece of reduced fineness should be coined and made unlimited legal tender, the existing eight-anna coins being withdrawn from circulation for recoinage at the reduced fineness. The practice of issuing subordinate coins of reduced fineness has been followed in the coinage of France and of the United States, and it seems to me much preferable to the use of nickel for such a high valued coin as the eight-anna piece in India.

43. The authorities in raising the rate of exchange were no doubt influenced by the difficulties there would have been in settling the balance of trade by other means than silver, and especially gold. But I venture to question whether they had the right, by executive action, to disturb the legally established money system. The people of India are accustomed to complaints from financial quarters about India's absorption of gold, but they were fairly entitled to expect that their rights in the money standard would have been protected so far as the Government authorities were concerned.

44. Also, it is difficult to see where the advantage lies in making the rate of exchange follow the price of silver. If silver has to be bought at present prices and coined into rupees at the present rate of exchange there is no economy of any consequence in using silver instead of gold. One of the advantages claimed in former years for issuing rupees instead of sovereigns was that it was economical. The rise in the price of silver took away that advantage.

45. I deal later with some of the objections raised to Indian demands for gold, but here I may point out that there is some misapprehension on the subject. The foreign trade of India is normally conducted with 77 other countries. From the following statement which I had supplied to the Indian press it will be seen that in the year 1913-14 (which was the last normal year before the war) the trade with each country resulted in a balance against India in the case of only five principal countries, the total adverse balance being 47,807,900*l.*, of which the principal one, the United Kingdom, had a balance due by India of 40,098,800*l.* All the other countries trading with India had to pay over 88,462,300*l.* to India. When, therefore, India takes gold it is because gold as the inter-

national form of money is due to her in payment of commodities supplied to those other countries.

Countries.	Exports of Merchandise from India.	Imports of Merchandise into India.	Balance of Trade against India.	Balance of Trade in favour of India.
	£	£	£	£
United Kingdom	38.234,300	78,333,100	40,098,800	...
Java, Borneo and Sumatra	1,415,500	7,773,900	6,358,400	...
Mauritius and Dependencies	867,700	1,635,100	817,400	...
Norway and Sweden	...	497,400	497,400	...
Persia	438,800	474,700	35,900	...
Japan	15,124,400	3,187,700	...	11,936,700
United States of America	14,518,100	3,186,100	...	11,332,000
France	11,711,500	1,794,900	...	9,916,600
Germany	16,867,800	8,452,000	...	8,415,800
Ceylon	5,866,300	548,100	...	5,318,200
Belgium	8,008,400	2,839,000	...	5,169,400
Hong Kong	5,102,300	654,900	...	4,447,400
Italy	5,219,000	1,478,100	...	3,740,900
Austria-Hungary	6,408,800	2,844,800	...	3,564,000
South America	3,181,800	800	...	3.181,000
Egypt	3,202,700	199,700	..	3,003,000
Australasia and Oceania	3,321,500	651,600	...	2,669,900
China Treaty Ports	3,799,200	1,136,700	...	2,662,500
Straits Settlements	4,367.500	2.293,200	...	2,074,300
Russia	1,636,200	37,700	...	1,598,500
Spain	1 479,200	...	...	1,479,200
Turkey in Asia	1,782,900	379,200	...	1,403,700
Holland	2.359,700	1,033,400	...	1,326,300
Canada	952,000	...	...	952,000
West Indies	561,900	...	...	561,900
Natal	535,100	...	...	535,100
Aden Dependencies	816,200	286,700	...	529,500
Indo-China	509,400	...	...	509,400
East African Ports	542,000	66,600	...	475,400
Siam	621,900	185,300	...	436,600

Countries.	Exports of Merchandise from India.	Imports of Merchandise into India.	Balance of Trade against India.	Balance of Trade in favour of India.
	£	£	£	£
Arabia	796,400	383,100	...	413,300
British East Africa	506,000	258,900	...	247,100
Cape Colony	243,700	...	...	243,700
Portuguese East Africa	331,100	100,500	...	230,600
Turkey in Europe	70,800	...	...	70,800
Other Countries	1,421,400	1,403,900	...	17,500
TOTAL	162,821,500	122,167,100	47,807,900	88,462,300

IV.—*The Requirements of Trade.*

46. The Committee were further asked to make recommendations as to the policy that should be pursued with a view to meeting the requirements of trade and to maintaining a satisfactory monetary circulation. It is very easy to exaggerate the importance of meeting the requirements of trade. Trade elsewhere is accustomed to finding its requirements met without the active intervention of Governments by means of sales of Government bills. The usual and correct attitude of Governments is to provide machinery for coinage and to leave it to its own automatic action, except for the provision of subsidiary coins. There seems to be no good reason for trade with India to be conducted on different lines from those followed by other advanced countries. The requirements of trade in this connection consist of finding the means of exchanging foreign money for Indian goods to satisfy the needs of the moment. Trade as such is not concerned with currency policy or with the economic effect produced by the method of carrying out its exchanges. Its concern is purely personal and temporary to see each transaction completed. The concern of the Government on the other hand should be to protect and safeguard the interests of the people as a whole in the maintenance of the legally settled standard, and I consider that Government would be performing its duty better by paying more attention to this aspect of the question than by showing anxiety for trade requirements. It is no doubt a convenience for banks and some of the public to be able to get Government rupee bills for making remittances to India, and, when required, also from India. But it is not a convenience that trade has any right to look for. So far as the Secretary of State has to sell bills to meet Government's own requirements, the practice of offering the bills for sale is unobjectionable. But that is not the case when bills are sold in excess of Government's own needs and without limit of amount on the ground that such sales meet trade

requirements. The real reason for this latter practice is not so much to meet the convenience of trade as to retain the power of diverting payments of India's foreign balances from gold to silver.

V.—*The Gold Exchange Standard.*

47. The Committee were further asked to make recommendations as to the policy which should be pursued with a view to ensuring a stable gold exchange standard.

48. Before examining the working of the gold exchange standard I think it desirable to refer to some of the objections raised to the Indian money system.

49. The Governor of the Bank of England in the very important evidence he gave before the Committee, while he disclaimed any knowledge of Indian conditions, commented freely on the money methods practised in India. This criticism, coming from the highest currency authority in England, calls for careful consideration. A few of what appear to me to be his principal objections may be stated.

50. He took exception to the medium of exchange (gold) being used as a vehicle for hoarding instead of being left to play its part in the regulation of the exchanges. It was a wasteful employment of gold and detrimental to the interests of the individuals who practised it and to those of India as a whole. He thought it would be much more to the interests of India as a whole that her favourable trade balances should be invested in some productive form abroad, as Great Britain used to settle her favourable balances by investing them in foreign interest-bearing securities. He also thought the Imperial Government would have some grounds for imposing restrictions upon the unlimited demand of India for gold in satisfaction of the balance of trade, and also because India had managed with reduced supplies of gold during the war he thought she ought to be able to continue to do so. For internal circulation notes, he said, were as good as gold, as the experience during the war had proved in England, and all the gold that was required was the amount likely to be withdrawn for export by presenting notes.

51. From these opinions it is clear that the Governor of the Bank thinks that India should economise the use of gold on the same lines as those followed in England. This is not the place to discuss the merits and demerits of the English system, but since it is put forward as an example for India to follow it seems necessary to say that, so far as the economy of gold in the internal circulation is concerned, the greatest agency in securing it has been the deposit-cheque system which originated with the bankers and their customers, apart from, and it is sometimes said in spite of, the Government or legal system of currency. Also, the methods by which the internal economy of gold for circulation purposes was attained in England developed simultaneously with the growth of the method of cancelling or avoiding gold imports in settlement of favourable foreign exchanges by means of foreign investments.

52. With regard to the suitability of this system for India, it seems necessary also to draw attention to the psychological difference between the people of India and the people of England. The people of India are a subject people with a history of many centuries behind them of insecurity of private property. They have been driven by the force of circumstances in the past to secrete as far as possible such property as they valued. The British people, on the other hand, have a long, proud record of insular security. They are an independent race, and their enterprise has carried them all over the world, where they have formed connections and found favourable investments to the great advantage of individuals and of their mother-country. If, therefore, the British people have themselves, independently of their Government, been successful in developing currency measures which have economised gold so satisfactorily to themselves, this mush very largely be attributed to their national characteristics and their historical sense of security. It cannot necessarily follow that the same gold economising measures are suitable to India, where the people have different traditions.

53. So far as the objectionable hoarding of gold is concerned there is not only the old tradition of insecurity of property inducing them to hoard, but there is the comparatively new form of internal token currency, not exchangeable into gold, which makes a very strong additional inducement to those who can afford it to hoard gold for security, as explained in a later paragraph.

54. In the matter of internal currency, India has nevertheless made considerable progress in the direction of following English currency methods, particularly in the form of notes and cheques, although she is a long way from economising to the same extent as in England in the metallic backing to cheques.

55. But while India still requires, and must require for a long time to come, a very solid metallic backing for her credit currency, that is not to say that she requires constant additions to her metallic currency merely because her trade balances are favourable. When the Governor of the Bank of England suggested that India should follow the English practice of settling favourable foreign balances by investments abroad, he touched the weakest spot in the administration of the Indian currency system, and pointed the way to the real remedy to avoid excessive demands for the precious metals and particularly gold. The policy has been to sell rupee bills on India in London without limit of amount, which meant to any extent that might be necessary to settle the trade balances, and while the policy did not exclude Indian investments abroad, it left the matter to individual initiative, and did nothing to favour or encourage such investments. Yet, if the objections raised to the absorption of the precious metals in adjustment of trade balances are to be satisfactorily met, it can only be by means of investments abroad by India, or, which is very much the same thing, by other countries borrowing in India.

56. The war afforded a favourable opportunity for getting India into the way of absorbing favourable trade balances by lending to Great Britain, an opportunity of which advantage was not taken. It may be said that India had some difficulty in raising the loan of 100 millions which she voluntarily contributed to the cost of the war. There was not the same inducement in that case that there would have been in the case of a loan offered by the British Government, and the rate of interest offered was not so good as the interest paid in some cases for similar public loans raised elsewhere by the Imperial Government. India is full of money, and notwithstanding the general idea that it is not available for investment, in my opinion it is a question of terms and security.

57. Since the wide break in the standard ratio between rupees and the sovereign with its attendant unsettlement and feeling of insecurity, there is now less chance of India seeking investments abroad than ever. There are in addition to the instability and insecurity of the money standard, questions connected with foreign investments which must scare Indian capital, such questions, for example, as foreign taxation, capital levies, and inflated values due to artificially-inflated currencies. But the same results, so far as the settlement of exchanges are concerned, could be obtained by the raising of foreign and particularly British loans in India.

58. Under the present system it can no doubt be claimed that India does in fact lend abroad through the investments held against the paper currency issue. But in so far as such investments represent either a forced loan from the people of India free of interest, or a tax on the money of the Indian people as explained later, they are not free of objections. I hardly think the Governor of the Bank had such loans in view when he made his suggestion as to India investing abroad.

59. Coming now to the working of the gold exchange standard, it seems necessary to mention the fact that the Indian money standard has been the subject of constant public controversy for many years. I have already referred to the difference of opinion as to whether it was a gold standard or a gold exchange standard. But the mere fact that there is any opening for this controversy is, by itself, a most undesirable and unsettling feature in money affairs. The standard should be so fixed and defined as to leave no possibility of dispute or question as to what it really is. As already stated, I take the view that the legally-established money standard is the sovereign with rupees definitely related to the sovereign at the rate of 15 to 1.

60. In contradistinction to this legally-established standard, the gold exchange standard has no legal validity. It has not been clearly and explicitly defined. The authorities who conduct it exercise the widest discretion in its regulation, but hitherto have been careful to respect the legally-constituted ratio between rupees and the sovereign. Its usual working characteristics are well known. In one direction the object aimed at is to provide absolute

security for the convertibility into sterling of so much of the internal currency as may be required for the settlement of India's external obligations. In the opposite direction it undertakes to sell rupee bills on India without limit of amount. In aiming at the maintenance of the sterling exchange it resembles the English system which, before the war, made a point of seeing that the exchanges remained within the gold points. In undertaking to sell rupee bills on India without limit the gold exchange standard system is unlike the English model, which, by means of the Bank rate, restricted expansion in the volume of internal credit currency and made it dependent upon the extent of the gold reserves.

61. The undertaking to provide rupees which are token coins without limit of amount, may in one sense be considered as authorised by the circumstance that rupees equally with sovereigns and half-sovereigns are full legal tender. Under the old silver standard rupees were, of course, legal tender, and when the standard was altered it was necessary to continue them as legal tender because of the great quantity which was then in circulation. But whether, from the point of view of the statutory standard of the sovereign, the tremendous volume of rupees which has been added to the token currency can be justified is another matter. In reality the endless issue of token coins, much in excess of what is needed for internal exchange purposes, amounts to a form of taxation on the money of the public. It is this circumstance that is to a very large extent responsible for the extraordinary demands for gold and sovereigns in India. It virtually compels the Indian people to seek full value for the token money with which they have been over-supplied for ordinary currency purposes, and is thus largely responsible for the hoarding of gold of which so much is heard. India's hidden stores of gold can never be expected to be used profitably for the benefit of the holders or of the State so long as no reasonable assurance is provided that, when used, they will remain a gold asset, and that assurance is not provided by a currency in circulation entirely composed of or based upon token coins.

62. When I say that the issue of rupees largely in excess of what is needed for ordinary internal exchanges constitutes a form of taxation on the money of the public, it is necessary to add that the difference between the cost of gold coins and silver coins, which is the amount of the tax, does not go into the Indian Treasury balances, but goes to form gold or invested reserves in London which are intended to meet remittances from India at a fixed rate which cannot be made so advantageously through other channels. But even if the profits on coinage went to swell the revenues of the Government they would be no less open to the very serious objection that they really formed a tax on the money of the public.

63. In present circumstances, however, this form of taxation has practically ceased, since the coinage of rupees at the moment is not profitable. But as a counter-balance to the virtual disappearance of this tax, the latest development of the gold exchange standard system has, by raising the rate of exchange and breaking

away from the statutory standard ratio, depreciated the commercial value in rupees of the whole of the rupee currency which has already been taxed.

64. This latest development gives ground for the gravest anxiety, not only on account of the depreciation in value of the immense volume of the rupee currency, but also because it means a revolution in the financial and economic life of India.

65. It alters as it were by a stroke of the pen, the existing relations between creditors and debtors. It cuts down the value in rupees of all existing holdings of the precious metals in India relatively to their value in the markets of the world, including the gold portion of the reserves held against the note issue, and, similarly, it cuts down the value in rupees of all existing and future stocks of Indian produce, and through this effect on the value of produce it is bound to prejudicially affect scores of millions of Indians engaged in agriculture, whose struggle for existence is already most severe. It is not too much to say that it will threaten the very existence of millions of such people. It will further handicap Indian industries in competition with similar industries abroad, and will severely check the prosperity of India. No doubt there will be some compensation. The finance of the Government will be relieved so long as the rate of exchange remains high, since the home remittances will cost considerably less in rupees, and it will be an advantage to those who buy imported goods or have payments to make outside of India.

66. It has been urged that one beneficial consequence will be the lowering of the high price level in India. This may be granted since the value in rupees of Indian produce, the price of which is ruled by outside markets, must fall. But it is nevertheless a questionable method of reducing prices. There has been no artificial inflation of the currency. Inflation of the currency has been a genuine inflation in India caused by a surplus of sales over purchases abroad. Even the forced loan in the paper currency issue is represented by debts due by the British Government. By the change in the standard ratio prices will be brought down, since prices are reckoned in rupees; but there is not the same good reason for changing the standard money to reduce prices that there is for deflating an artificially inflated currency to obtain the same result. In my opinion the inflation of currency in India is the consequence rather than the cause of high prices. The currency has been inflated because the balance of trade was favourable and because additions to the currency were the normal way of settling trade balances. The balance of trade was increased by the increased prices paid for commodities for export. In this way the additions to the currency were a consequence of high prices. On the other hand the inflation of currency cannot in its turn be held to have raised prices, since all accounts go to show that currency of all kinds has been hoarded on a very large scale, and hoarded money does not act on prices. The change in the standard ratio will bring down rupee prices, but it will leave undisturbed the real cause of the high prices in India,

which was that world prices were high and world prices were high mainly because the currencies of many countries were artificially inflated. It is simply a case of altering the nature of the money in which prices are reckoned, and, when advanced in excuse for the change of ratio, can only be regarded as an argument to deceive the people.

67. The effect of the change outside of India cannot be so clearly estimated. But the probabilities are that with the higher sterling cost of the rupee the demand for Indian produce will fall off, while remittances from India being cheaper in rupees imports will be stimulated. If these probabilities should materialise India's trade balances will become less favourable to her than they have been, or it may be the trade balances will turn against her. In either event the London market, where India's international trade is mostly financed and finally adjusted, will be relieved of the necessity of settling India's trade balances by means of specie remittances to the same extent as formerly, if indeed specie remittances to India will be necessary at all, while in addition to that advantage the stimulation of imports by the reduced rupee cost of sterling exchange will increase the demand for English textile manufactures.

68. These revolutionary changes in the Indian money system should not have been possible and much less necessary at a time when immense sums were due to India in exchange for her commodities. They are to be explained by the particular bent of the policy followed—a policy of making India accept payment in India of the balances due to her as far as possible in the form of rupees. A policy less rigidly bent in that direction would have been susceptible to the need for meeting the very special circumstances of the time by other methods, such, for example, as that suggested by the Governor of the Bank of England when he pointed out the desirability of investments abroad in settlement of India's foreign claims. It is a policy which has persistently ignored the essential safeguards of a gold standard, and particularly the safeguard of limiting the issue of token coins. It has by mere executive action changed the legally-established gold standard into a gold exchange standard, making the maintenance of exchange the object to be attained in place of the provision of gold money with a limitation of token money. And while the maintenance of exchange was the main object, the policy has broken away from the normal rate of exchange on the ground that the rise in the price of silver rendered that course necessary, although, as I have endeavoured to show, there was no real necessity for doing so. The fact that the maintenance of exchange was so readily abandoned and the sale of rupee bills continued, combined with the persistent flooding of India with silver token money, gives ground for the theory that fixity of exchange was only the ostensible object of the policy, and that the real object was to compel India to take silver in place of gold money. Further, it is a policy which is settled and managed in London, and which necessarily operates in the markets of London

and India. That the interests of the London market have not been without influence in shaping the policy may be gathered from the enormous sums of money or investments belonging to the Indian currency which have been accumulated there. The profits on silver coinage were steadily collected into the gold standard reserves in London, and now that the coinage of silver has ceased to be profitable, a new departure has been made in the issue of currency notes in India on the security of investments in London, which has had the effect of rapidly accumulating an enormously increased store of Indian currency money in London. These are changes which will be viewed in India with the gravest concern and mistrust.

69. India is fairly entitled to a system of sound money. The gold exchange standard has failed to provide such a system, and I am unable to make any recommendations for its continuance which would secure the stability it has lost. I consider that the authorities had no right to take the action of raising the rate of exchange and, in my opinion, it is their duty to proceed to undo what they have done.

VI.—*Policy.*

70. On the subject of policy I desire to associate myself generally with the views expressed in the following extract from the able memorandum submitted to the Committee by Sir Stanley Reed, Kt., K.B.E., LL.D., of Bombay:—

> "......... I am strongly of opinion that the control now excercised by the Secretary of State over the Indian exchanges should be abolished at once. Official control over the exchanges is always a bad thing, and whilst possibly justified under the immense strain of the war, should not be retained a moment longer than is absolutely necessary. It has already been abolished in every other country in the world, and it should be abolished in the case of India with the minimum of delay. Whilst this is true as a financial proposition, it is specially true of a country in the political condition of India. The Government of India, and to no less a degree the Secretary of State, is suspect in the eyes of a large section of the Indian community. All its actions are jealously regarded, often misunderstood, no less frequently misrepresented. The Secretary of State operates 6,000 miles from the great Indian financial centres. He is surrounded by, and naturally amenable to, interests which are not Indian in their ideas and aims. He acts in secret, and it is frequently impossible to obtain any information in India of the groundwork of measures which, however wise and expedient in themselves are not understood and are liable to perversion in India itself. The political disadvantages of such complete powers being exercised in secret so far from the people who are vitally affected by them, cannot easily be exaggerated. The only remedy is for the Secretary

of State to divest himself as completely as possible from the management of the Indian currency and exchanges, and to allow these to be governed by normal conditions. It is essential, therefore, that the fixing of the exchanges by the Secretary of State and the distribution of Council bills amongst a limited circle of 'approved' buyers should not be restored. Council bills should be sold by open tender to whomsoever may apply, the only limitation being the smallest amount to be tendered, which might be retained at the figure of 10,000 rupees. Whatever inconveniences may attach to this procedure will be outweighed by the practical advantage of freeing the Secretary of State from the suspicion which, however unwarranted, is widely entertained, of subordinating the interests of India to those of financial institutions in the City of London, and of giving banks with their headquarters in London a preference over banks with their headquarters in India.

The first of these essential steps is to remove all restrictions on the free movement of gold and silver bullion to and from India, and to establish free and unfettered trade in both precious metals. It is the inalienable right of every creditor country to determine for itself the form in which its debts shall be paid. India is a creditor country and will remain a creditor country for as far ahead as we can see. India is a bullion-using country, and the present exchange and currency difficulties have largely arisen from the arrest of the normal flow of gold to India and the substitution of credits abroad by Government for the liquidation of the large balance of trade. Deprived of the normal supply of gold bullion, India has turned to the only precious metal available, and has absorbed coined rupees in prodigious quantities. There can be no financial health in India until this traditional demand for bullion is satisfied. The Currency Commission of 1913, presided over by Mr. Austen Chamberlain, laid down that 'the extent to which India should use gold must, in our opinion, be decided solely in accordance with India's own needs and wishes, and it appears to us to be just as unjust as to force gold coins into circulation in India on the ground that such action will benefit the gold-using countries of the rest of the world, as it would be to attempt to refuse to India facilities for obtaining gold in order to prevent what adherents of the opposite school have called the drain of gold to India.' The demand for freedom of trade for India in the precious metals comes from every important financial and commercial authority in the land, and it must be boldly and unequivocably recognised.

It is objected that India is a bottomless sink for the absorption of the precious metals, and that gold once passed into general consumption in India is permanently lost to the rest of the world. This attempt to fasten upon India an exceptional and invidious responsibility for the consumption of gold cannot be too vigorously combated. India is still an illiterate

country, whose credit and banking facilities are miserably unorganised and where the practice of holding small savings in gold and silver ornaments is centuries old. Yet its normal demand for the industrial arts, and for the satisfaction of the social customs of three hundred and fifteen millions of people, was met before the war by about ten millions of gold annually. The United States of America was reported recently to be absorbing a million sterling in gold per month for industrial purposes. Yet no one says that the United States is a bottomless sink in the matter of her gold absorption. It is stated that in England one of the most flourishing trades during the war was that in cheap jewellery, in which form the working classes invested a substantial proportion of their increased earnings. Every country in the world uses gold and silver for industrial and domestic purposes, and it induces a sense of angry injustice to find that the Indian demand for the precious metals, for precisely the same purposes, is perverted into senseless hoarding, especially when the history and conditions would justify a far larger gold absorption than the Western nations with their general literacy and highly organised credit systems can claim.

The success of these and any other measures which may be adopted will largely depend on the publicity with which they are carried into effect.

Attention has already been drawn to the particularly difficult task which the Government of India has to discharge owing to the political status of India. That political status inevitably exposes all the acts of the Government of India to distrust, misrepresentation, and prejudice. Whilst this is true of the Government of India, which is in close contact with Indian opinion, whose members are well known in all commercial and financial centres, and where successive Finance Ministers have made it a practice for a number of years to keep in personal touch with financial and commercial opinion, it is doubly true of the Secretary of State, the final authority in all financial matters affecting India, who operates six thousand miles away, remote from Indian thought, feeling, and influence, but in living contact with the London market. Experience has taught us that the only remedy for misunderstanding in India is publicity; the antidote to misunderstanding and distrust is the truth. A mountain of misunderstanding of the most regrettable character, involving political dangers of great magnitude, has been reared by the secrecy with which the Secretary of State controls Indian financial policy: this mountain can be levelled only by the truth, spread with the widest publicity. It follows, then, that all financial operations carried on by the Secretary of State should be conducted in public, and that the path of wisdom lies in the Secretary of State divesting himself so far as possible from the management of the Indian currency and exchanges, and substituting for this management automatic operations carried out in the gaze of the public.

An important step in this direction will have been taken if a free, open, and automatic exchange is established, Council bills being sold to the highest tenderers. But it will be necessary to supplement this measure by others in the same direction. All purchases of silver for the Government of India should be by open tender to be delivered in Bombay. Quite apart from the fact that this will attract to the great bullion market of Bombay silver from all parts of the world, it is the only means whereby the cloud of suspicion which overhangs the purchases of silver for the Government of India can be dispersed. The returns relating to all operations—currency and exchange—undertaken by or for the Government of India, should be couched in the fullest possible form and published at frequent and regular intervals. The financial position of India is such that she has nothing to fear from publicity: publicity is the great instrument through which to strengthen her credit abroad, and the position of the Government of India at home. *Magna est veritas, et prævalebit*—but truth cannot prevail if it is interred in the archives of the India Office."

Ancillary Problems.

Duty on Imported Silver.

71. In my opinion the duty charged on silver imported into India is closely connected with the currency policy, and is calculated to deter the economic advancement of the people of India. This is a question which is not of importance so long as the embargo on private imports of silver is maintained, and no duty is consequently being levied. But when the embargo is raised I suggest that the duty should be given up because it is, in effect, a levy on the petty savings of multitudes of the people. The practice which custom impels the Indian masses to place such small cash reserves as they can scrape together in unfruitful investments in silver ornaments is, of course, a matter for regret, but it is simply a continuance of long established custom on the part of poor and ignorant classes whose individual accumulations are very small, and, as a form of savings, not a fit subject for taxation.

72. It has to be remembered that the Indian masses were for long accustomed to see the values of silver, and of rupees on an equality. They could at any time convert their silver ornaments into rupees with little loss. With the closing of the Mints to the free coinage of silver this traditional equality of silver with rupees was broken. Rupees became of more value than silver. That change by itself was startling enough to the poorer and uneducated classes, but while it had the effect of depreciating the value in rupees of their holdings of silver, it gave them the opportunity of putting future savings into the customary form of silver at an advantageous rate relatively to rupees. To this great change in the position of silver relatively to rupees there came to be added another innovation in the form of an import duty on silver, which meant that

everyone who followed the usual custom of purchasing silver was called upon to pay a contribution to the State. The amount of the duty is a minor consideration. It is the fact of the duty being levied which is objectionable, for if the principle of a duty is admitted there is always the risk of the duty being expanded, and that has already happened.

73. The great alteration caused in the rupee valuation of silver by the change in the monetary standard from silver to gold, followed by the duty on silver imports, cut right into the established traditions and habits of the masses in the matter of their savings; but while there was good reason for the change in the standard, there seems to me to be no sufficient reason for the silver duty. It is not calculated to inspire the masses with a sense of fairness on the part of Government towards their monetary habits, and on that account, is, I consider, likely to retard their economic advancement on sounder lines.

74. The duty on silver as carried out in practice is objectionable in other ways. When imported silver is re-exported the duty paid on importation cannot be recovered in full, thus placing an unfair burden on the Indian purchaser. In consequence of this inability to recover the duty in full on re-exports, the Indian silver market is placed at a disadvantage in competition with silver markets elsewhere, leading frequently to silver being retained in India when it might be re-exported. This disadvantage to the market reacts on holders of silver when they have occasion to dispose of their holdings, because, although they have paid the duty at the time of purchase, they may find when they come to sell that purchasers will deduct the duty from the market price on the ground that the silver may have to be sold abroad in competition with other silver markets.

India's Banking Problem.

75. India has an area of 1,802,657 square miles, and it contains 2,253 towns with 29,748,228 inhabitants and 720,342 villages with a population of 285,406,168. On the 31st December, 1917, the total number of banking offices in India was only 402, and many of them overlapped in the larger towns. In fact, on that date there were in the whole of India only 165 towns which had bank offices. The United Kingdom, with a population of 48,000,000, had 9,138 banking offices. Canada, with a population of 8,460,000, has about 4,000 branches of banks. Further, there are 294,875,000 illiterate people in India, and out of the 18,539,578 literates there are only 1,670,387 literates in English.

76. The vast and scattered population of India has thus modern banking facilities at 165 stations only, and consequently the financial power of India is insufficiently mobilised. Money lies dormant in endless small hoards.

77. It will be seen that there is a vast virgin field for the development and expansion of banking and for the collection into bank reserves of the innumerable stores of money lying idle throughout the country which could be utilised for the benefit of the holders

and for the good of trade and of the State. At the same time expansion must necessarily be slow. The Indian public cannot be hurried and hustled in such matters.

78. It is sometimes said that a greater development of banking would cure the currency troubles. That seems to me to be putting the cart before the horse. The first essential to a great extension of modern banking is a currency system which inspires the public with absolute confidence. A credit system cannot overcome the difficulties arising from a system of money which is liable to violent changes in the valuation of the different forms of money of which it is composed, such as the present alteration in the ratio of rupees to the sovereign. No credit system could cure that fault in the money on which it rests. On the contrary, unsound money would imperil the credit system. Hence, in my opinion, the need for making the money system in India a specially strong and sound one if the money resources of India are ever to be mobilised in a great banking system.

79. In conclusion, I desire to add my tribute to the great ability and courtesy with which the Secretaries, Messrs. Kisch and Denning, have discharged their duties.

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